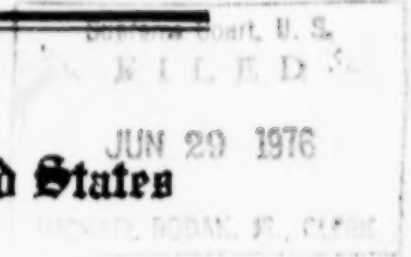


No. 75-1889

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IN THE  
**Supreme Court of the United States**  
OCTOBER TERM, 1975

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COMMONWEALTH OF PENNSYLVANIA and  
NEW YORK STATE DEPARTMENT OF TRANSPORTATION,  
*Petitioners,*

v.

INTERSTATE COMMERCE COMMISSION, *et al.*,  
*Respondents.*

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PETITION FOR A WRIT OF CERTIORARI TO  
THE UNITED STATES COURT OF APPEALS FOR  
THE DISTRICT OF COLUMBIA CIRCUIT

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COMMONWEALTH OF PENNSYLVANIA and  
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*Petitioners,*

v.

INTERSTATE COMMERCE COMMISSION, *et al.*,  
*Respondents.*

\_\_\_\_\_  
**PETITION FOR A WRIT OF CERTIORARI TO  
THE UNITED STATES COURT OF APPEALS FOR  
THE DISTRICT OF COLUMBIA CIRCUIT**  
\_\_\_\_\_

Petitioners, Commonwealth of Pennsylvania, and New York State Department of Transportation, respectfully pray that a writ of certiorari issue to review the judgment and opinion of the United States Court of Appeals for the District of Columbia Circuit, entered in this proceeding on March 31, 1976.

### OPINIONS BELOW

The opinion of the U.S. Court of Appeals is not yet reported, and is reproduced in the Appendix hereto. (App. 1a-21a).

The regulations of the Interstate Commerce Commission promulgated in its Ex Parte No. 293 (Sub-No. 2), *Standards for Determining Rail Service Continuation Subsidies*, were issued January 8, 1975, 40 Fed. Reg. 1624 (App. 24a-46a), as corrected, 40 Fed. Reg. 3216 (App. 47a-48a), and subsequently amended March 28, 1975, upon petitions for reconsideration. 40 Fed. Reg. 14186 (App. 49a-57a).

### JURISDICTION

The judgment of the U.S. Court of Appeals was entered March 31, 1976 (App. 22a-23a). The jurisdiction of this Court is conferred by 28 U.S.C. 1254(1), 2101(c).

### QUESTION PRESENTED

Whether the Interstate Commerce Commission's determination of standards to be used in conjunction with expedited discontinuance of rail service, and also for rail service continuation subsidies, under Sections 205(d)(6) and 304 of Regional Rail Reorganization Act of 1973, as amended, is inconsistent with the terms of that Act.

### STATUTES INVOLVED

The statutes primarily involved are Section 205(d)(6), Section 304(a)(2), and Section 304(c)(2)(A), of Regional Rail Reorganization Act of 1973, as amended, 45 U.S.C. 715(d)(6), 744(a)(2), 744(c)(2)(A):<sup>1</sup>

#### Section 205(d)(6) (90 Stat. 59):

(d) DUTIES.—In addition to its duties and responsibilities under other provisions of this Act and under the Railroad Revitalization and Regulatory Reform Act of 1976, the Office shall —

\* \* \*

(6) determine and publish, and from time to time revise and reissue, standards for determining (A) the 'revenue attributable to the rail properties', (B) the 'avoidable cost of providing service,' (C) a 'reasonable return on the value', and (D) a 'reasonable management fee', as those phrases are used in Section 304 of this Act, after a proceeding in accordance with the provisions of Section 553 of Title 5, United States Code;

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<sup>1</sup> These sections of the Rail Act were amended by Sections 309 and 804 of Railroad Revitalization and Regulatory Reform Act of 1976, enacted February 5, 1976 (P.L. 94-210). The statutory language shown embraces these amendments, and was considered by the court below.



Section 304(a)(2) (90 Stat. 133-34):

(a) DISCONTINUANCE —

“(2)(A) If rail properties are not, in accordance with the designations in the final system plan, required to be operated, as a consequence of a recommended arrangement for joint use or operation of rail properties (under section 206(g) of this Act) or as part of a coordination project (under sections 206(c) and (g) of this Act), rail service on such properties may be discontinued, subsequent to the date of conveyance of rail properties pursuant to such section 303(b)(1), if the Commission determines that such rail service on such rail properties is not compensatory and if—

“(i) the petitioner and any other railroad involved in such arrangement or coordination project have, prior to filing an application for such discontinuance, entered into a binding agreement (effective on or before the effective date of such discontinuance) to carry out such arrangement or project;

“(ii) such application is filed with the Commission not later than 1 year after the effective date of the final system plan; and

“(iii) such discontinuance is not precluded by the terms of the leases and agreements referred to in such section 303(b)(2).

“(B) For purposes of this paragraph, rail service on rail properties is compensatory if the revenue attributable to such properties from such service equals or exceeds the sum of the avoidable costs of providing such service on such properties plus a reasonable return on the value of such rail properties, as determined in accordance with the standards developed pursuant to section 205(d)(6) of the Act.

“(C) The Commission shall make its final determination, with respect to any discontinuance requested under this paragraph, not later than 120 days after the date of filing of an application therefor. The applicant shall have the burden of proving that the service involved is not compensatory. If the Commission fails to make a final determination within such time, the application shall be deemed to be granted.

“(D) The Commission may issue such rules, regulations, and procedures as it deems necessary for the conduct of its functions under this paragraph.

Section 304(c)(2) (90 Stat. 134-35):

(c) CONTINUATION OF RAIL SERVICES—  
No rail service may be discontinued and no rail properties may be abandoned, pursuant to this section —

(2) if a financially responsible person (including a government entity) offers —

(A) to provide a rail service continuation payment which is designed to cover the difference between the revenue attributable to such rail properties and the avoidable costs of providing rail service on such properties, together with a reasonable return on the value of such properties;

### STATEMENT

This case involves the attack by Pennsylvania and New York upon the validity of regulations promulgated by the Interstate Commerce Commission (I.C.C.), through its Rail Services Planning Office ("RSPO"), which set the standards for determining three key terms employed in Regional Rail Reorganization Act of 1973, ("Rail Act"), as amended. The three terms, "revenue attributable", "avoidable cost", and "reasonable return", provide the basis for determining whether expedited abandonments are to be allowed by the I.C.C. in certain instances, and also the level of subsidy to be advanced by a State or by a "responsible person" for the continuation of rail service. The regulations primarily involve branch line operation.

Pennsylvania and New York challenge the standards for "avoidable cost", but do not quarrel with the I.C.C.'s decision for "revenue attributable" or for "reasonable return." In the court below, the trustee for The Central Railroad Company of New Jersey, sought review of the I.C.C.'s determination of "reasonable return", and its proceeding was consolidated with the States' petition for review. The Court below sustained the regulations under the statute, but deferred to the Special Court, established under section 209 of the Rail Act, as to questions of constitutionality. (App. 3a-4a).

The States' primary disagreement with the I.C.C.'s formulation of "avoidable cost" of service on a branch line is the I.C.C.'s inclusion of "off-branch" costs to be assessed against operation on the branch line.

United States Railway Association on July 26, 1975, promulgated its Final System Plan, under which some 7,000 miles of railroad line in the Northeast would be excluded from future operation.<sup>2</sup> The Final System Plan became operative November 9, 1975, when neither the House or Senate passed a resolution of disapproval. 45 U.S.C. 718.

The Rail Act was substantially amended by enactment of Railroad Revitalization and Regulatory Reform Act of 1976 on February 5, 1976. (P.L. No. 94-210). The conveyance and transfer of rail properties was consummated April 1, 1976.

The I.C.C.'s regulations were issued January 8, 1975, as amended March 28, 1975. (App. 24a-57a). They were issued pursuant to section 205(d)(3) of the Rail Act as it then stood, which required the I.C.C. to determine, in a rulemaking proceeding, standards for determining "revenue attributable", "avoidable cost", and "reasonable return". Subsequently, the section was amended to embrace "reasonable management fee", but no issues are involved at this time with respect to "reasonable management fee".<sup>3</sup> These phrases

<sup>2</sup> S. Rept. No. 94-499 on S. 2718, *Rail Services Act of 1975*, (Nov. 26, 1975), at p. 42; H. Rept. No. 94-725 on H.R. 10979, *Rail Revitalization and Regulatory Reform Act of 1975*, (Dec. 12, 1975), at p. 96.

<sup>3</sup> The "reasonable management fee" was added by section 309 of P.L. No. 94-210, and is the subject of pending rulemaking. 41 Fed. Reg. 8468.

are tied to section 304 of the Rail Act, which governs expedited discontinuance of rail service, as well as rail continuation subsidies, primarily for branch lines.

Section 205(d)(3) of the Rail Act now reads, as renumbered section 205(d)(6) and as amended:

“determine and publish, and from time to time revise and reissue, standards for determining (A) ‘revenue attributable to the rail properties’, (B) the ‘avoidable cost of providing service’, (C) a ‘reasonable return on the value’, and (D) a ‘reasonable management fee’, as those phrases are used in section 304 of this Act, after a proceeding in accordance with the provisions of section 553 of title 5, United States Code.”

Section 205(d)(6) is patterned after legislation enacted in 1970 involving rail passenger service. Congress assigned the task of determining “revenues attributable” and “avoidable cost” to the I.C.C. in the Rail Passenger Service Act. 45 U.S.C. 502(6):

“‘Avoidable loss’ means the avoidable costs of providing passenger service, less revenue attributable thereto, as determined by the Interstate Commerce Commission pursuant to the provisions of section 553 of title 5, United States Code.”

The I.C.C. issued regulations for “revenue attributable” and “avoidable costs” under the Rail Passenger Service Act. *Losses Under the Rail Pass. Act. of 1970*, 343 I.C.C. 379 (1973). Under these regulations, the I.C.C. allocated both revenues and costs to the particular service.

Moreover, the I.C.C. over the years in its rail line abandonment proceedings, has evolved standards for attributing revenue to a branch line proposed for abandonment, and for determining the avoidable costs for the branch line.<sup>4</sup>

Despite this background, in the instant case the I.C.C. determined to include substantial “off-branch” costs in calculating the avoidable cost of service on the branch itself, thus inflating costs. On the other hand, the I.C.C. attributed 100 percent of a railroad’s freight revenue to the branch if the shipment originated or terminated on the branch, while the I.C.C. continued to allocate passenger revenue. (App. 31a, 39a-40a, 57a).

The I.C.C. in its decision justified its departure from the norms established under the Rail Passenger Service Act, and in prior abandonment cases, on the ground that avoidable costs under the Rail Act are concerned with retaining service, rather than with abandoning service. (App. 31a):

“The Office agrees that the phrase “avoidable cost” should be strictly construed, but this fact does not necessarily exclude indirect costs. It is important to note that the Act discusses avoidable costs in the context of *providing* the service not of *abandoning* the service.”

---

<sup>4</sup> In general, the revenues credited to the branch line for a given shipment consist of a mileage prorate of the revenue as between the branch and the system, with 50 percent of the system revenue then added to the branch for “feeder value”. Against this revenue are the avoidable costs of operating the branch line, without any specific computation of so-called “off-branch” costs. See: *Moeller v. Interstate Commerce Commission*, 201 F. Supp. 583, 587 (S.D. Ia. 1962). This 50 percent rule is criticized by New York and others as too low, and that a higher percentage is justified. *Penn Central Abandonment*, 347 I.C.C. 223 (1971).



The Court of Appeals sustained the I.C.C.'s decision, although it recognized the force of the States' contentions (App. 5a):

"We recognize the force of the contentions in the petition filed by the States. But there are important countervailing considerations."

The Court of Appeals stated that the I.C.C.'s definition of "avoidable cost" in this situation was "a novel one" but that a word "takes on the hue of its surroundings" (App. 6a). The Court noted the reasoning of the I.C.C. in the context and legislative purpose of the Rail Act, but did not rely upon it as the complete answer. Rather, the Court stated that the I.C.C. has expressed doubt, prior to enactment of the 1970 Passenger Act, as to difficulties associated with a determination of "avoidable costs" for passenger train service. The Court added that "a basic reality", in a passenger-freight separation, is that revenues are wholly severable, whereas the calculation of branch revenues from a run that is part on-branch and part off-branch requires a comparison of costs and revenues, and that the only presently practicable way of taking this into account is to assign to the branch line all revenues earned by traffic originating or terminating on the branch, and correspondingly, to determine the quantum of off-branch of system costs in producing such revenues (App. 10a).

The court concluded that its decision was without prejudice to reconsideration in light of particularized factual showing as to the consequences of the regulations (App. 11a-12a).

## REASONS FOR GRANTING THE WRIT

### THE DETERMINATION OF RAILROAD BRANCH LINE SUBSIDY PAYMENTS IS AN IMPORTANT NATIONAL ISSUE

This case is of great importance to the nation as well as to Pennsylvania and New York, two of the principal states involved in the Northeast railroad reorganization. About 1,000 miles of railroad branch lines presently are under subsidy contracts between these two states and the railroads, principally with Consolidated Rail Corporation.

This current rail service continuation arrangement in which Pennsylvania and New York participate, provides for 100 percent federal funding during the first 12-month period subsequent to the conveyance of rail properties under section 303(b)(1) of the Rail Act, and 90 percent funding for the succeeding 12-month period. (P.L. 94-210, section 805). The rail properties were conveyed April 1, 1976. This subsidy arrangement terminates two years from conveyance. (P.L. 94-210, section 806).

The rail subsidy program is not restricted to the Northeast states. Congress in P.L. 94-210, on February 5, 1976, extended the program nationwide. The same 100 percent and 90 percent formulation for the first two years, applies to light-density rail lines in states outside the Northeast region, commencing July 1, 1976. The Northeast states become eligible for the national program when the special Northeast two-year period expires March 31, 1978. (P.L. 94-210, section 803).

The federal share of the subsidy drops to 80 percent for the third year, which ends June 30, 1979, and further to 70 percent for the following two years ending June 30, 1981. (P.L. 94-210, section 803).

The I.C.C.'s treatment of avoidable costs is critical to the entire nation.

The Rail Act, as amended in 1976, marks a new departure in federal railroad policy. Freight service on light-density lines is to be subsidized by federal-state programs, whereas heretofore a branch was allowed to be abandoned if operations thereon constituted an undue burden on interstate commerce. See: Cherington, Charles R., *The Regulation of Railroad Abandonments*, (Harvard, 1948); Conant, Michael, *Railroad Mergers and Abandonments* (U. of Calif., 1964).

**1. There Is No Difference Between Avoidable Cost for Providing Service and Avoidable Cost by Abandoning Service.**

The I.C.C. erred in adopting a "novel" definition of avoidable cost, and which is an "anomaly" in view of the prior use of the term. (App. 6a). The I.C.C. reasoned that its formula was to be used for *providing* freight service, whereas previous usage of avoidable cost was for *abandoning* the service. (App. 31a). Thus, in the present case, the cost formula saddles subsidizers with substantial "off-branch" costs, whereas traditional cost computations excluded the calculation of such costs.

There is no basis in the statutory language for such a cost distinction between providing and abandoning service. The statutory language in section 205(d)(6) was taken from the Rail Passenger Service Act, 45 U.S.C. 502(6), and Congress had the I.C.C.'s "avoidable cost" and "revenue attributable" standards before it when it had the Rail Act under consideration. *Losses Under the Rail Pass. Serv. Act of 1970*, 343 I.C.C. 379 (1973).

There is nothing in the legislative history to suggest a different meaning for "avoidable cost" than its prior usage. The Senate committee report clearly considered "avoidable cost" to be "directly attributable" or "solely related" to the particular service. S. Rept. No. 93-601 on S. 2767, *Rail Services Act of 1973*, at p. 37 (Dec. 6, 1973).

The 1976 amendments to section 304 of the Rail Act reaffirmed the lack of any distinction between the avoidable cost of continuing service compared with the avoidable cost to be saved by abandonment.

Whereas Section 304 previously required the consideration of avoidable cost, as calculated under section 205(d)(6), only for rail continuation subsidies, section 304(a) as amended by P.L. 94-210 now requires the use of avoidable cost to determine whether certain service is not compensatory, and thus a candidate for discontinuance. Such avoidable cost for the discontinuance provision of section 304 directly and specifically comes under the standards in issue here which are established by the I.C.C. in section 205(d)(6). Section 304(a), governing discontinuances, spells this out in paragraph (2)(B):

"For purposes of this paragraph, rail service on rail properties is compensatory if the revenue attributable to such properties from such service equals or exceeds the sum of the avoidable costs of providing such service on such properties plus a reasonable return on the value of such properties, as determined in accordance with the standards developed pursuant to section 205(d)(6) of this Act."

The statement by the Court of Appeals that the 1976 amendment did not make any material change in the provisions of section 304(b) or (c) is correct; however, the



court below apparently overlooked the significant and major revision in section 304(a). (App. 15a-17a).

Finally, we point out that the distinction between the cost showing necessary for *providing* rail service and *abandoning* rail service has no logical base. When the I.C.C. in its abandonment or discontinuance cases, concluded to deny a carrier's request predicated upon the avoidable cost showing, the effect of the agency's decision was to require that the railroad continue to provide the service.

## 2. The Court of Appeals Erred in Claiming Petitioners Would Not Be Harmed Under the I.C.C.'s Regulations.

The Court of Appeals erred in its statement that these petitioners, Pennsylvania and New York, along with other potential subsidizers, would not be harmed since the federal government assumed 100 percent of the subsidy in the initial year, and that particularized objections can be raised later. (App. 11a-12a).

Pennsylvania and New York are harmed by the I.C.C.'s regulations, which inflate the required subsidy, even though 100 percent of the operating subsidy may be federally funded, because such funds come out of the total entitlement to the State under section 402 of the Rail Act, 45 U.S.C. 762, which thereby diminishes funds available to the State under that section for maintaining main lines, for assisting other rail facilities, and for rail planning activities.

The I.C.C.'s regulations have an immediate effect upon Pennsylvania and New York, and are facially invalid, such that relief should not await particular situations.

## 3. The I.C.C. Can Formulate Standards for Determining Avoidable Costs.

The court below erred in assuming that avoidable costs were beyond the expertise or capability of the I.C.C. (App. 10a-12a). To be sure, the I.C.C. may have advised Congress in 1970, prior to enactment of Rail Passenger Service Act, that problems are encountered in measuring avoidable costs, as mentioned by the court. (App. 10a). Nevertheless, Congress still required the I.C.C. to determine such "avoidable costs," and the I.C.C. performed the task under the passenger service legislation.

There is no indication that the I.C.C.'s job is now "impossible" as suggested by the court below. (App. 11a). Indeed, if this were the case, the I.C.C. should have so advised the Congress.

We believe the Court below has too lightly acquitted the I.C.C. of its duty, and that the court itself recognized that the standards adopted here by the agency represented a sharp departure from prior practice in deriving the standards for "avoidable cost."

CONCLUSION

For these reasons, a writ of certiorari should issue to review the judgment and opinion of the United States Court of Appeals for the District of Columbia Circuit in this case.

Respectfully submitted,

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June, 1976

Notice: This opinion is subject to formal revision before publication in the Federal Reporter or U.S. App. D.C. Reports. Users are requested to notify the Clerk of any formal errors in order that corrections may be made before the bound volumes go to press.

APPENDIX A

**United States Court of Appeals**

FOR THE DISTRICT OF COLUMBIA CIRCUIT

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No. 75-1529

COMMONWEALTH OF PENNSYLVANIA AND NEW YORK  
STATE DEPARTMENT OF TRANSPORTATION, PETITIONERS

v.

INTERSTATE COMMERCE COMMISSION AND UNITED STATES  
OF AMERICA, RESPONDENTS

---

No. 75-1762

R. D. TIMPANY, TRUSTEE IN REORGANIZATION OF THE  
CENTRAL RAILROAD COMPANY OF NEW JERSEY, PETITIONER

v.

RAIL SERVICES PLANNING OFFICE, INTERSTATE COMMERCE  
COMMISSION AND UNITED STATES, RESPONDENTS

STATE OF NEW JERSEY DEPARTMENT OF TRANSPORTATION,  
COMMISSIONER OF TRANSPORTATION OF THE STATE OF  
NEW YORK COMMONWEALTH OF PENNSYLVANIA &  
RAYMOND T. SCHULER, INTERVENORS

---

Petition for Review and Cross-Application for  
Enforcement of an order of the Interstate  
Commerce Commission

---

Argued March 4, 1976

Decided March 31, 1976

*Gordon P. MacDougall*, Special Assistant Attorney General, Commonwealth of Pennsylvania for petitioner, Commonwealth of Pennsylvania in No. 75-1529 and intervenor Commonwealth of Pennsylvania in No. 75-1762.

*John C. McTiernan* for petitioner, New York State Department of Transportation in No. 75-1529 and intervenor Commissioner of Transportation of the State of New York in No. 75-1762.

*Stanley Weiss* for petitioner in No. 75-1762.

*Henri F. Rush*, Attorney, Interstate Commerce Commission, with whom *Fritz R. Kahn*, General Counsel, Interstate Commerce Commission, *John H. D. Wigger* and *John H. Broadley*, Attorneys, Department of Justice, were on the brief for respondents. *Peter A. Fitzpatrick* Attorney, Interstate Commerce Commission also entered an appearance for respondent, Interstate Commerce Commission.

*Kenneth S. Levy* for intervenor State of New Jersey Department of Transportation in No. 75-1762.

Before: LEVENTHAL, ROBINSON and ROBB, *Circuit Judges*

Opinion for the Court filed by *Circuit Judge LEVENTHAL*.

LEVENTHAL, *Circuit Judge*: This case presents petitions to review an order of the Rail Services Planning Office (RSPO) of the Interstate Commerce Commission (ICC) which promulgated legislative regulations<sup>1</sup> pursuant to § 205(d) of the Regional Rail Reorganization Act of 1974, as amended, 45 U.S.C. § 715(d) (Act). The order set forth standards for determining rail service continuation subsidies, to govern rail properties not transferred to the Consolidated Rail Corporation (Conrail)

<sup>1</sup> 49 C.F.R. § 1125, published in 40 F.R. 1624-36 (Jan. 8, 1975), as amended, 40 F.R. 14186-90 (March 28, 1975).

under the Final System Plan developed pursuant to the Act.

This case was argued on March 4, 1976. It was put on an expedited briefing and argument schedule, in view of the imminence and significance of the April 1, 1976, date set by the Act, as amended in 1976, for transfer of rail properties, and the clear intent of Congress to facilitate continued rail operation and service to the public with respect to both the properties designated for transfer to Conrail and those subject to the rail service continuation subsidy processes of the Act.<sup>2</sup> These same concerns prompt us to render this decision in an expedited fashion, stating only the highlights of our reasoning.

1. The court is of the view that it does not have jurisdiction to decide the claim of R.D. Timpany, trustee in reorganization of the Central Railroad Company of New Jersey, that the Act authorizes RSPO "to establish standards for determining a reasonable rate of return on value" in violation of its constitutional right to "a judicial determination of just compensation for its property taken by eminent domain."<sup>3</sup> No jurisdictional issue

<sup>2</sup> As to the premium put on timely implementation of the Final System Plan and the relegation of controversies over payment for the properties to post-conveyance procedures, see, e.g., H. R. REP. NO. 620, 93d Cong., 1st Sess. 54-55 (1973). The 1976 Amendments make clear a similar concern with respect to rail properties not included in the Final System Plan. Thus, in order "to prevent any disruption or loss of rail service at any time after the date of conveyance," § 304(d) of the Act, as amended, Pub. L. 94-210, 90 Stat. 31, 106, § 804 (Feb. 5, 1976), authorizes the ICC "to direct rail service to be provided by any designated railroad or by the trustees of a railroad in reorganization in the region, if a rail service continuation payment has been offered but an applicable operating or lease agreement is not in effect." The ICC issued such an order on March 16, 1976.

<sup>3</sup> Brief of Petitioner in No. 75-1762 at ix (issue 4). Trustee Timpany's petition for review does not contain an attack on



has been raised, and apparently this court did have jurisdiction of the case, under 28 U.S.C. §§ 2321, 2342, as amended, Pub. L. 93-584, 88 Stat. 1917, §§ 4-5 (Jan. 2, 1975), when the briefs were filed during October-December 1975. But as we read § 602(b) of the 1976 amendments, Pub. L. 94-210, 90 Stat. 31, 86 (Feb. 5, 1976), the Special Court, established pursuant to the Act, has been given original and exclusive jurisdiction over civil actions "challenging the constitutionality of this Act or any provision thereof. . . ."

2. The court does have jurisdiction to consider the various contentions in the petitions to review, allegations filed by Timpany and by the States of Pennsylvania and New York, that the regulations of the RSPO are invalid under the governing statute. These regulations pertain to the situation of lines or segments of lines not desired by Conrail as part of its permanent system, but which are so situated that "a financially responsible person"—for the most part states or state agencies—desires continuation of service, at least during a transitional period, and is willing to offer a rail service continuation subsidy sufficient to cover the difference between the "avoidable costs of providing service" on such properties and the "revenues attributable" to the properties plus a "reasonable return on the value" of the properties. Section 304 (c) of the Act, 45 U.S.C. § 744(c), prohibits the discontinuance of rail service and abandonment of rail properties where such a subsidy is offered in conformance with the statutory formula, the operative terms of which are determined by RSPO standards issued pursuant to § 205(d) (3) of the Act, *id.* § 715(d) (3). The challenges in the instant petitions are to RSPO's definition of the terms "avoidable costs" and "reasonable return on value."

the constitutionality of the Act as such, although such a contention may be subsumed under the claim that RSPO's regulations are "violative of the Fifth Amendment of the Constitution of the United States." Appendix on Behalf of Petitioner in No. 75-1762 at 86a.

Section 304(b)-(c) of the Act and the pertinent provisions of the regulations are set forth in an Appendix to this opinion.

3. Pennsylvania and New York attack as contrary to the Act RSPO's definition of "avoidable costs" to include off-branch costs. We decline to hold the RSPO regulations invalid on their face. We recognize the force of the contentions in the petition filed by the States. But there are important countervailing considerations.

The States' principal contention is that Congress in 1974 adopted by reference the usage of the ICC in its regulations implementing the Rail Passenger Service Act of 1970, 45 U.S.C. §§ 501 ff. The 1970 statute required the ICC to develop regulations for the determination of "avoidable losses" which would apply in the event of impasse between the National Railroad Passenger Corporation (Amtrak) and a railroad as to the final settlement price to be paid to Amtrak by the railroad, which was shifting over its loss-incurring passenger service responsibility. The railroad's "avoidable loss" for 1969, defined by the statute to mean "the avoidable costs of providing passenger service, less revenues attributable thereto," as those terms would be further elaborated by the ICC, provided one of the two bases for the final settlement price.<sup>4</sup> The ICC definitions, apparently keying "avoidable loss" to the "avoidable costs" of providing the

<sup>4</sup> Consideration for relief from the carrier's responsibility to provide the service could be either (1) three years of payment of an amount equal to one-third of 50 percent of the fully distributed passenger service deficit of the railroad as reported to the ICC for the year ending December 31, 1969, or (2) 100 percent of the avoidable loss of all intercity rail passenger service operated by the railroad during the period from January 1, 1969, to December 31, 1969 (or 200 percent of the avoidable losses during the same period for intercity service over the routes that Amtrak would actually operate). 45 U.S.C. § 561(a) (2)-(3).



specific passenger service to be abandoned, are set out in the margin.<sup>5</sup>

There is implicit recognition in the RSPO regulations that its definition of "avoidable costs" was a novel one, and this presents something of an anomaly since the same words—"avoidable costs"—are used by Congress in both statutes. But a word "is not a crystal, transparent and unchanged," and it takes on the hue of its surroundings, so that the same word may mean different things in different sections of the same statute, and certainly in different, though related, statutes. *Towne v. Eisner*, 245 U.S. 418, 425 (1918); *Lamar v. United States*, 240 U.S. 60, 65 (1916). RSPO justified its formulation by noting that the difference in approach was responsive to a difference in context—a shift from payment by carriers enabled to discontinue service, to a subsidy payment to carriers for continued operation. In the interest of time we quote the RSPO's somewhat technical analysis in a footnote, without our restatement.<sup>6</sup> While we do not have

<sup>5</sup> § 1123.2 Definitions.

(a) Avoidable costs are those operating expenses, rents, and taxes listed in the Uniform System of Accounts (title 49 CFR 1200-1201) which can be demonstrated to have been required for the provision of intercity rail passenger service in 1969, which would not have been incurred had such service not been performed.

(b) Avoidable loss is the excess of avoidable costs of providing intercity rail passenger service over the non-retainable revenues from the same service, pursuant to section 102 (6) of the Rail Passenger Service Act of 1970.

\* \* \* \*

(d) Solely related expenses are the operating expenses, rents, and taxes which are incurred only for providing a specific service.

<sup>6</sup> RSPO's approach can be gleaned from the following extracts of its discussion of the positions of the various parties:

[Continued]

<sup>6</sup> [Continued]

The estimate for "revenues attributable" will include the same sources of revenues as those required in the standards. These include freight and passenger revenues from all traffic originated or terminated on the branch, existing subsidy payments, overhead traffic and accessorial revenues. All of the data will be presented for the same base year as employed by the Association in the decision-making process (presumably 1973). These data may be adjusted for rate changes. By agreement of the parties, more current figures may be used.

A ratio of the off-branch costs to revenues for the base year will be calculated for each branch. The ratio will be applied to the estimated revenue for the subsidy year to determine the estimated off-branch cost. The off-branch calculation will utilize variable system average costs, short line mileages, and traffic information from the waybill abstract files. The Office will computerize the formula and make the calculations available to interested parties.

(40 F.R. 1626).

\* \* \* \*

The widest range of disagreement between the petitioners arises in the discussion concerning the cost accounts to be included in the standards. Basically, the parties representing railroad interests support full allocation of all costs. The potential subsidizers takes the position that the standards should exclude indirect costs.

The Office agrees that the phrase "avoidable cost" should be strictly construed, but this fact does not necessarily exclude indirect costs. It is important to note that the Act discusses avoidable costs in the context of *providing* the service not of *abandoning* the service. This distinction is significant. Equipment depreciation accounts best illustrate this distinction. As many parties suggest, capital investment is a "sunk cost" and the depreciation thereof, taken from the viewpoint of abandonment, is not an avoidable cost. However, when viewed from the standpoint of a continuing operation, capital investments in equipment must be made from time to time in order to maintain service; and, consequently, depreciation costs for these items would be avoidable. The same principle

the familiarity with the subject matter that permits expert understanding of the matter, we do have the perception that under the 1970 measure the carrier was paying a one-shot settlement price for terminating the particular service, so that there was room for rigidity in saying that the amount it saved thereby (to be paid to the quasi-public corporation, Amtrak) would be determined completely without regard to the separated service that was being continued by the carrier, and that there is a distinctly different situation when the two services are being continued and integrated by the same operator (Conrail).

would also apply to structure depreciation, but, the standards provide that rehabilitation costs be recovered during the period covered by the subsidy agreement. In effect, capital investment in structures is treated as an expense. Each on-branch account has been reviewed and the modifications reflected in the amended standards are summarized below.

(*id.* 1627).

\* \* \* \*

Some parties challenged the use of the functional service unit costs developed by the application of Rail Form A, as the basis of determining off-branch costs since it utilizes variable costs. They suggest that Rail Form A was not designed to develop avoidable costs and that its use for that purpose is improper. While on the surface it might seem inconsistent to allow system variable costs to be allowed for off-branch costs, it is believed justified on the basis of equity to the railroad since all system revenues from traffic originating or terminating on the branch are attributed to the branch. A failure to recognize off-branch variable costs would probably lead to situations where the operating railroad would try to divert the traffic to another carrier at the earliest possible point regardless of service considerations. This would not only result in circuitous movement and concomitant time delays but would also decrease the revenue attributable to the branch. The adopted approach recognizes the services rendered by the carrier to the branch traffic.

(*id.* 1628).

There is also a difference in legislative purpose. Under the 1970 Act, the emphasis was to take reasonable steps to prevent the departing carrier from obtaining what might be termed an unjust enrichment in giving up its legal burden to provide intercity passenger service. Under the 1974 Act, the emphasis is on reasonable steps to assure that there is an accurate allocation of the burden of continuing short-line rail operations which were not designated for transfer to Conrail under the Final System Plan but which are desired to be continued by the potential subsidizer.

These differences in context and legislative purpose seem pertinent to us, but we do not rely on them as the complete answer. The legislative history of the 1974 Act on the "avoidable cost" concept, cited to us by petitioners, refers to the "costs directly attributable or solely related to the costs of a particular service, but would not include any portion of the common costs which would not be covered by revenues received by reason of operation of a line." S. Rep. No. 93-601, 93d Cong., 1st Sess. 37 (1973). But we are not referred to anything in the legislative history that requires that these costs be measured by duplication of the ICC regulations under the 1970 law.<sup>9a</sup>

<sup>9a</sup> Although not cited to us by counsel, we are not unaware that the House bill, H.R. 9142, used the language "fully distributed costs of handling traffic on such rail properties" in place of the "avoidable costs" concept, but that the conference substitute which was ultimately enacted incorporated the "avoidable costs" language of the Senate amendment. H. Rep. No. 93-744, 93d Cong., 1st Sess. 61-63 (1973). However, there is no indication in the Senate and Conference Committee reports of reliance on the 1970 statute or the ICC regulations thereunder. What this legislative history suggests is that Congress intended a clear nexus between the revenues attributable to the particular line and the costs incurred in their production, to exclude "any portion of the common costs which would not be covered by revenues received by operation of a line." In our view, and on the basis of the present record, the RSPO regulation is a reasonable attempt at such a calculation. See pp. 10-11 *infra*.



Indeed, as the Government points out, it is unlikely that Congress intended RSPO to duplicate ICC usage, since the ICC had prior to the passage of the 1970 Act expressed serious doubt as to whether existing accounting practices were sufficiently refined "to permit the ascertainment of all avoidable costs associated with discontinuance cases," S. Rep. No. 91-765, 91st Cong., 2d Sess. 39-40 (1970), and the participating railroads had found the "avoidable loss" concept sufficiently unworkable to elect a potentially more expensive basis for making payments to Amtrak.<sup>7</sup>

The question remains whether the RSPO regulations comport with the legislative intent that "avoidable costs" be "directly attributable" or "solely related" to the line or service involved. The petition of the States argues that the RSPO has presented a more liberal view of "avoidable costs," entailing a greater charge on the states seeking to subsidize short-line operations, than Congress intended. Our approach is shaped by what we see as a basic reality, that RSPO was confronted with the obvious fact that unlike the passenger-freight separation under the 1970 Act, where revenues are wholly severable, any calculation of branch revenues from a run that is part on-branch and part off-branch requires some attention to the relationship of both elements. In RSPO's view, the "avoidable costs" of a branch line require a comparison of costs and revenues; and the only presently practicable way of taking this into account is to assign to the branch line all revenues earned by traffic originating or terminating on the branch, and correspondingly to determine the quantum of off-branch or system costs in producing such revenues. The Government contends that since fixed overhead costs are excluded from RSPO's definition, the only

<sup>7</sup> Joint Brief of the United States of America, ICC & RSPO at 58-60.

off-branch or system costs attributed to the branch line are those which are unquestionably increased as a result of handling cars originating or terminating on the branch line and are thus "directly attributable" to producing the "revenues received by operation of the line."<sup>8</sup>

The opposing States have not countered RSPO's determination that their suggested alternatives would either be too expensive (a system-wide accounting and reporting system) or too complex to administer (an approach based on the per diem regulations of the ICC<sup>9</sup>), and have not shown that RSPO's approach will require a significantly greater expenditure of state revenues for rail service continuation subsidies than the approaches they advocate. We cannot assume that Congress intended RSPO to accomplish the impossible. And there may be impossibility in substance and in effect even when something can be achieved, but at a cost that wholly outweighs any conceivable benefit. A French proverb cautions that the best should not be the enemy of the good. It is reasonable to assume that Congress did not intend the infeasible perfect to oust the feasible good. *Cf. Environmental Defense Fund, Inc. v. EPA*, 167 U.S.App.D.C. 71, 77, 510 F.2d 1292, 1298 (1975).

Finally, it counts with us—and we make this explicit to avoid any possible misunderstanding—that as of this juncture we can reject, and do reject, the contention of the petition filed by the States that the RSPO regulation is facially invalid, without prejudice to reconsideration in light of a particularized factual showing as to the consequences of the regulation. We take account of the

<sup>8</sup> *Id.* at 61.

<sup>9</sup> RSPO found that while a system-wide accounting and reporting system might be desirable "one cannot be justified on the basis of the subsidy program alone," 40 F.R. 1626; and that an approach requiring the identification of car-miles and car-days by car type and application of the per diem rate by car type "would be overly complex to apply" and that the ICC per-diem rates "contain an element of profit," *id.* 14188.

fact that RSPO sees its approach as interim methodology to set the rail subsidy program in operation, 40 F.R. 1626, and that the regulations themselves make provision for adjustment at the end of the initial subsidy year to reflect the results of actual operation, 49 C.F.R. § 1125.8 (f). We also note that petitioner States and other potential subsidizers will not be harmed if the "avoidable costs" standards prove too generous during the initial subsidy year, for as a result of the 1976 amendments the Federal Government will pay 100 percent of the subsidy.<sup>10</sup>

4. The regulations are attacked by Timpany, as trustee in reorganization of the Central Railroad Company of New Jersey, on essentially two grounds.<sup>11</sup> First, the Act prohibits the owner of the railroad from abandoning his road and yet does not give him just compensation for the use of the road, as determined in a judicial proceeding. Second, RSPO's determination in its regulations to premise the "reasonable return on value" component of the subsidies on "net liquidation value," rather than some purportedly fairer basis which takes into account the "assemblage" value of an established rail corridor, sets an unconstitutionally low standard and is contrary to congressional intent.

<sup>10</sup> The Federal share is 90 percent for the second subsidy year. Then the program changes, and the 17 states in the Northeast/Midwest Region join a national rail service continuation assistance program, in which states are entitled to funds in proportion to their total rail mileage eligible for assistance. Pub. L. 94-210, 90 Stat. 31, 109-13 §§ 805-806 (Feb. 5, 1976).

<sup>11</sup> Petitioner Timpany also challenges RSPO's authority under the Act to determine the content of a notice of intent to discontinue rail service, and in particular the requirement that cost data be collected and made available for public inspection. We reject this contention as wholly lacking in merit. It is clearly within the delegation of authority to RSPO to ensure the orderly implementation of the subsidy program by requiring railroads obtaining subsidies to collect information necessary to judgments as to future subsidization.

In general, the issues as to the constitutionality of the § 304(c) procedures and that of the relationship between "net liquidation value" and "fair value" overlap and are questions primarily for development by the Special Court. Putting aside doubts as to our jurisdiction, we see no basis for interjection by this court to enjoin or interfere with the regulations. As Timpany's brief recognizes (at pp. 7-8, 34-36), "net liquidation value" may be "fair value" in some factual settings, although perhaps not in others. The gist of petitioner's complaint is that RSPO has promulgated an inexorable rule of compensation for a "taking" which will fall short of the constitutional minimum in many cases. In our view, petitioner overstates his plight, and his challenge is premature. The regulation's standards are essentially guidelines for resolving through compulsory arbitration impasses between potential subsidizers and the owners of the short-line roads. The regulations have immediate impact in terms of outlining the amounts payable by the states in the event of impasse in negotiations with the carriers. The carrier is temporarily deprived of the right to abandon short-line operations during the period of the subsidy program, with the fee remaining in the estate. If the statute operates to require the owner to make his road available, to lease it, as it were, without the fair return provided by the Constitution—an issue as to which we express no opinion—the contention is one that can be presented to the Court of Claims under the Tucker Act, 28 U.S.C. § 1491. This is a fair corollary of the ruling of the Supreme Court, *Regional Rail Reorganization Act Cases*, 419 U.S. 102 (1974), adopting the approach of the Special Court, *In Re Penn Central Transportation Co.*, 384 F. Supp. 895 (1974).<sup>12</sup>

\* \* \*

<sup>12</sup> Although RSPO envisions arbitration along the lines of its subsidy standards to be final and binding "as to the meaning of these standards," 40 F.R. 1629, this does not, and



It may be appropriate to add a word on review jurisdiction and venue. This is perhaps the first, but it may well not be the last, case where an ICC order is interrelated with the matters under active consideration by the Special Court, but is reviewable under present statutes in the circuit courts of appeals. There are obvious reasons why a court as busy as the Special Court should not be saddled with possibly over-extensive exclusive jurisdiction. But perhaps there would be a benefit if Congress permitted a transfer jurisdiction, whereby an appropriate case may be transferred from the generalist circuit court of appeals, where the petition to review has been filed, to the Special Court (a district court), if the Special Court accepts the transfer.

The petitions for review are denied.

*So ordered.*

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cannot, negate the holding of the Supreme Court and Special Court that Congress by the 1974 Act did not withdraw the Tucker Act remedy ordinarily available for "takings" without "just compensation."

Apparently, the Special Court has been given authority to make awards reflecting the constitutional concerns identified in its opinion. The 1976 amendments empower the Special Court in passing on the fairness and equity of transfers or conveyances pursuant to the Final System Plan to "tak[e] into consideration compensable unconstitutional erosion, if any"; and to include in the "certificates of value" issued to those transferring rail property to Conrail "such amount, if any, as the special court may determine shall be required after taking into consideration compensable unconstitutional erosion, if any," which may occur during bankruptcy proceedings. Pub. L. 94-210, 90 Stat. 31, 75, 81, §§ 610(b), 612(q) (Feb. 5, 1976). These provisions do not pertain to the situation of the short-line roads involved in this case, which were not designated for transfer to Conrail.

## APPENDIX

Section 304(b) and (c) of the Regional Rail Reorganization Act of 1974, 45 U.S.C. §§ 744(b)-(c) provided:

(b) Abandonment.—(1) Rail properties over which rail service has been discontinued under subsection (a) of this section may not be abandoned sooner than 120 days after the effective date of such discontinuance except as provided in subsections (c) and (f) of this section. Thereafter, except as provided in subsection (c) of this section, such rail properties may be abandoned upon 30 days' notice in writing to all those required to receive notice under paragraph (2)(C) of subsection (a) of this section.

(2) In any case in which rail properties proposed to be abandoned under this section are designated by the final system plan as rail properties which are suitable for use for other public purposes (including roads or highways, other forms of mass transportation, conservation, and recreation), such rail properties shall not be sold, leased, exchanged, or otherwise disposed of during the 180-day period beginning on the date of notice of proposed abandonment under this section unless such rail properties have first been offered, upon reasonable terms, for acquisition for public purposes.

(c) Limitations.—Rail service may be discontinued and rail properties may be abandoned under subsections (a) and (b) of this section notwithstanding any provision of the Interstate Commerce Act or the constitution or law of any State or the decision of any court or administrative agency of the United States or of any State. No rail service may be discontinued and no rail properties may be abandoned pursuant to this section—



(1) after 2 years from the effective date of the final system plan or more than 2 years after the final payment of any rail service continuation subsidy is received, whichever is later; or

(2) if a shipper, a State, the United States, a local or regional transportation authority, or any responsible person offers—

(A) a rail service continuation subsidy which covers the difference between the revenue attributable to such rail properties and the avoidable costs of providing service on such rail properties plus a reasonable return on the value of such rail properties;

(B) a rail service continuation subsidy which is payable pursuant to a lease or agreement with a State, or a local or regional transportation authority, under which financial support was being provided on January 2, 1974, for the continuance of rail passenger service; or

(C) to purchase, pursuant to subsection (d) of this section, such rail properties in order to operate rail service over such properties.

If a rail service continuation subsidy is offered, the government or person offering the subsidy shall enter into an operating agreement with the Corporation or any responsible person (including a government entity) under which the Corporation or such person (including a government entity) will operate rail service over such rail properties and receive the difference between the revenue attributable to such properties and the avoidable costs of providing service on such rail properties and the trustee of any railroad in reorganization shall receive a reasonable

rate of return on the value of any rail properties for which a rail service is operated under such subsidy.

The 1976 Amendments do not make any pertinent changes in these provisions.

\* \* \*

The provisions of the regulations issued by the Rail Services Planning Office (RSPO) (40 F.R. 1631 ff.) pertinent to this case are:

#### § 1125.3 Interim subsidy payment.

The person offering a subsidy shall offer to pay, in return for the continuation of rail service, an amount computed on the basis of the interim formula described in this section. The interim payment may be adjusted, by agreement of the parties, to take into account factors, such as rate increases and changes in traffic levels which would make the sole use of base year data an inappropriate means of estimating the payment for the subsidy year. The interim formula makes use of estimates of revenues, off-branch costs, on-branch costs and a return on the value of the properties involved. The "base year" for all estimates under this section shall be the same year employed by the United States Railway Association in developing the final system plan pursuant to sections 206 and 207 of the Act.

(a) *Revenues.* The estimated revenues shall include all the sources of revenue described in § 1125.4, computed on the basis of base year data.

(b) *Off-branch costs.* A ratio of off-branch costs to revenues for the base year shall be used to derive the estimate of the off-branch costs for the subsidy year. The base year off-branch costs shall be calculated using the methodology described in § 1125.5(k). If data identifying actual carloads by car type are not

available, car type shall be based upon the railroad's best estimate. A ratio shall be developed by applying these costs against the base year revenues. The resulting ratio shall be applied to the revenues estimated in paragraph (a) of this section to develop the estimated off-branch cost for the subsidy year.

#### § 1125.5 Avoidable costs of providing service.

The avoidable costs of providing service on a branch are the total of the costs assigned or apportioned to the branch in accordance with this section. All on-branch costs, whether direct or allocated, shall be computed separately for freight and passenger services. Costs apportioned under paragraphs (a) through (k) of this section shall be derived from the latest Form R-1 of the railroad filed with the Commission prior to the conclusion of the subsidy year. Labor costs must be identified separately for all accounts when costs are assigned on a direct basis.

\* \* \*

(k) *Off-branch costs.* (1) Certain terminal costs, line-haul car costs, and interchange costs shall be considered as the off-branch avoidable costs of providing service over the remainder of the railroad's system. These costs shall be computed by applying variable unit costs to the service units attributed to the branch traffic during the subsidy period.

(2) The following through train single line variable unit costs shall be developed by the railroad by applying data contained in its latest Form R-1 filed with the Commission to Rail Form A: cost per carload by car type, modified cost per carload by car type (substitute an intertrain switching cost, separated between mileage and other than mileage cars, for a road train to industry switching cost; and substitute a modified car ownership cost developed in

accordance with section 1125.5(j) above using an allowance of two days in the terminal to cover the loaded and empty car movement for the standard car ownership costs; cost per car-mile by car type; cost per ton-mile; and cost per car interchanged, separated between mileage cars and other than mileage cars.

(3) Terminal costs shall be calculated by multiplying the modified costs per carload, by car type, by the total number of carloads originated or terminated on the branch during the subsidy year. To this amount add the regular costs per carload, by car type, times the number of carloads which originate or terminate on the branch that are local to the railroad serving the branch.

(4) The line haul costs shall be calculated by applying the costs per car-mile by car type to the loaded car-miles on the system by car type originated or terminated on the branch during the subsidy year and applying the ton-mile unit cost to the total ton-miles on the system of revenue freight in road service originated or terminated on the branch during the subsidy year and totaling the results.

(5) The interchange costs shall be calculated by multiplying the cost per car interchanged by the number of carloads of traffic interchanged that originated or terminated on the branch.

#### § 1125.6 Valuation of rail properties.

The value of the rail properties on a branch shall be determined in accordance with the following:

(a) Only the following properties on a branch may be considered:



(1) Those that are used and useful to provide the rail services requested by the person offering a subsidy.

(2) In the absence of a request for specific services by that person, those properties that are used and useful to provide the rail service performed on the branch at the time the final system plan becomes effective, or if no service was being performed at that time, the services that were last performed on the branch.

(b) The value of the properties shall be their net liquidation value for their highest and best use, consistent with applicable zoning and land use regulations, determined by computing their current market value for other than rail transportation purposes, less all costs of dismantling and disposition of improvement necessary to make the remaining property available for its highest and best use.

(c) If the railroad and person offering a subsidy cannot, within a period of time that either of them considers reasonable after the beginning of negotiations for the payment of the subsidy, agree on the properties that are used and useful or the net liquidation value, or both, the one that considers that a reasonable period of time has elapsed may notify the other of its intention to have the matter arbitrated. Each of the parties shall then appoint a representative and the representatives shall select an arbitrator or arbitrators mutually acceptable to them. The decision of the arbitrator or arbitrators shall be final.

(d) If either party fails to appoint a representative within five days after receiving notice from the other party of its representative, or if the appointed representatives fail, within five days after the last

one of them is appointed, to agree upon a mutually acceptable arbitrator or arbitrators, either party may submit the matter for arbitration to the American Arbitration Association pursuant to its commercial arbitration rules, and the decision of its arbitrator or arbitrators shall be final.

(e) In considering the value of properties under this section, the arbitrator or arbitrators shall consider, among other factors, any bona fide offer for the properties, or a part thereof, recent sales of adjoining or similar properties, and any available appraisals, by a reputable appraiser, of the properties, or a part thereof.

(f) If the person offering a subsidy is a public body, each meeting of an arbitrator or arbitrators with the parties for the purposes of receiving information or evidence or to hear arguments or views shall be open to the public. Any interested member of the public may file written views, argument, or information with the arbitrator or arbitrators at any time within 3 days after the closing of the sessions that are open to the public.

**APPENDIX B**  
**UNITED STATES COURT OF APPEALS**  
**FOR THE DISTRICT OF COLUMBIA CIRCUIT**

No. 75-1529

September Term, 1975

Filed March 31, 1976

Commonwealth of Pennsylvania and New  
 York State Department of Transportation,  
 Petitioners

v.

Interstate Commerce Commission and United  
 State of America, Respondents

No. 75-1762

R. D. Timpany, Trustee in Reorganization  
 of the Central Railroad Company of New  
 Jersey, Petitioner

v.

Rail Services Planning Office, Interstate  
 Commerce Commission and United  
 States, Respondents

State of New Jersey Department of Trans-  
 portation, Commissioner of Transportation  
 of the State of New York, Commonwealth  
 of Pennsylvania & Raymond T. Schuler,  
 Intervenors

**PETITIONS FOR REVIEW AND CROSS APPLICATION FOR EN-  
 FORCEMENT OF AN ORDER OF THE INTERSTATE COMMERCE  
 COMMISSION**

Before: LEVENTHAL, ROBINSON and ROBB, Circuit  
 Judges

**JUDGMENT**

These causes came on to be heard on petitions for re-  
 view and cross-application for enforcement of an order of  
 the Interstate Commerce Commission and were argued by  
 counsel. On consideration of the foregoing, it is

ORDERED AND ADJUDGED by this Court that the  
 petitions for review are denied, in accordance with the  
 opinion of this Court filed herein this date.

Per Curiam  
 For the Court

/s/ George A. Fisher  
 George A. Fisher  
 Clerk

Date: March 31, 1976

Opinion for the Court filed by Circuit Judge Leventhal

## APPENDIX C

# INTERSTATE COMMERCE COMMISSION

## STANDARDS FOR DETERMINING RAIL SERVICE CONTINUATION SUBSIDIES

(January 8, 1975)  
(40 Fed. Reg. 1624)

## Title 49—Transportation

CHAPTER X—INTERSTATE COMMERCE  
COMMISSION

## SUBCHAPTER B—PRACTICE AND PROCEDURE

[Ex Parte No. 293 (Sub-No. 2)]

PART 1125—STANDARDS FOR DETER-  
MINING RAIL SERVICE CONTINUATION  
SUBSIDIES

On February 25, 1974 (39 FR 7182), the Director of the Rail Services Planning Office (Office) of the Interstate Commerce Commission (Commission) issued a notice of proposed rulemaking and order, pursuant to section 205(d)(3) of the Regional Rail Reorganization Act of 1973 ("Act") which provides that the Rail Services Planning Office shall:

• • • within 180 days after the date of enactment of this Act, determine and publish standards for determining the "revenue attributable to the rail properties," the "avoidable costs of providing service" and "a reasonable return on the value," as those phrases are used in section 304 of this Act, after a proceeding in accordance with the provisions of section 553 of Title 5, United States Code • • •

After an extended (113 days) period for public comment, the Office issued standards on July 1, 1974 (39 FR 24294).

The standards defined "revenue attributable" as the actual revenues accruing to the railroad as derived from waybills and other source documents, plus any subsidy payments that would cease on termination of service. Passenger revenues not directly assignable would be prorated on the basis of passenger miles on the branch to passenger miles.

The "avoidable costs of providing service" on the branch were defined as actual costs to the extent that they are available. Where they are not available, allocation formulas based upon the railroad's annual report form (R-1) filed with the Commission would be employed. Avoidable off-branch costs would be determined by a formula based on an application of system-wide data contained in the carrier's annual report (R-1) to the Commission's Formula for Use in Determining Rail Freight Service Costs, Rail Form A, Statement 1F1-73 (Rail Form A). Avoidable costs would also include the costs incurred in upgrading service and improving the condition of track and related facilities.

The calendar year before the year in which the notice of intent to discontinue service is filed was established as the base year for revenue and cost data, unless that notice were given prior to April 1 in which case it would be the second preceding calendar year.

The standards adopted July 1 defined "reasonable return" as the interest rate equal to the publicly quoted yield on U.S. Treasury notes of approximately the same life as the subsidy agreement. The value of the properties upon which the return would be based was defined as the net liquidation value of those properties used and useful to provide the service demanded by the person offering the subsidy; that is their current market value less the cost of dismantling and disposition. Disputes over what property is needed to provide service and over the value of that property would be settled by arbitration.

Notice of a proposal to discontinue service was required to be given to the general public by publication in local newspapers. Notice would also have to be given to the Governor and public service commission of each State in which the branch is located, and to the Office.

On July 30, 1974, the Office issued a notice announcing that petitions seeking amendment of the standards would be accepted if filed on or before August 19, 1974 (39 FR 28196).

During August and September the Office conducted a series of public seminars explaining the purpose of the standards and their applicability.

In requesting amendment of the standards, several parties urged that the standards be tested on actual branch lines, and that the time for filing pleadings seeking amendment of the standards be extended until such tests could be completed. On September 10, 1974, the Office issued a notice announcing that it would test the standards and that the time for filing pleadings was being extended to October 30, 1974. All interested parties were invited to participate in the tests (39 FR 33574).

The petitions for reconsideration, the public seminars, and the branch line tests revealed that the standards adopted on July 1 required modification in a number of respects, and they are being amended effective immediately. Since the revised standards reflect significant changes from the original version, public comments seeking further amendment will be entertained until February 18, 1975.

In recognition of the fact that the circumstances surrounding each subsidy situation are different, the revised standards are intended to encourage negotiations between the parties to structure subsidy agreements to meet those circumstances. It is believed that arm's-length negotiations between the parties will provide a better basis for a subsidy agreement than would rigid standards.



For example, the subsidizer may wish to provide funds to improve track conditions so that higher speed limits would be permitted. Higher speeds could, in some instances, result in lower transportation costs, and since transportation costs represent a significant portion of on-branch costs, it may be possible that this factor, during the subsidy period, would more than offset the rehabilitation costs. This would result in better overall service at a lower total cost.

It is also conceivable that adjustments in the frequency of service would be desired. In many situations reliability of service is more important to the shipper than frequency of service. While the latest regular service level will be established as the standard, an agreement between the parties to either raise or lower it will not be precluded. Other inducements, such as relief from revenue or property taxes, could also be taken into consideration in the negotiations. However, in the event an agreement cannot be reached on a voluntary basis, a mandatory procedure is provided to assure continuation of service.

#### BRANCH LINE TESTS

Each State within the 17-State region covered by the Act was requested to identify a branch line for test purposes. Initially, it was anticipated that tests would be conducted on each of the lines so identified. However, as a result of the initial tests, it was determined that further testing would be of little value since it was apparent that significant modification of the standards would be necessary.

The Office used the testing program as an opportunity to work together with interested parties in order to perfect the published standards and thus better fulfill the Office's responsibility under the Act. Points made in the petitions filed and at public seminars conducted by the Office were checked during the tests. Many of the modifications adopted herein result directly from information and knowledge obtained during the testing.

The standards were tested on two Penn Central Transportation Company lines: the line between Georgetown and Lewes, Delaware, and the line between Columbus and Holmesville, Ohio. On-site investigations were conducted to determine the availability of data required by the standards. As indicated above, notice of the tests was given through publication in the Federal Register and was served on all parties to this proceeding. All persons indicating a desire to participate were invited to attend.

The first trip was to Philadelphia, Pennsylvania, to inspect the records maintained at the Penn Central headquarters. The inspection revealed that Penn Central's accounting system is designed to accumulate data on a responsibility rather than territorial basis. It was found that the entire Penn Central rail system is divided into over 6,000 "responsibility" levels with each department (transportation, maintenance of way, etc.) having its own set of so-called management center accounts. In addition, it was found that the railroad's accounting system is flexible enough to collect costs for specific purposes.

Currently, Penn Central maintains approximately 2,000 "cost centers" covering activities involving financial agreements with other parties, e.g., leased lines, joint-use facilities and passenger operations. This cost system cuts across responsibility lines and provides direct cost for any activity so designated. It was found that through this system direct cost collection at the branch level could be initiated within approximately 30 days after a line had been designated and adequately described.

It was further learned that data is not collected in a systematized manner at the branch level for many of the factors involved in the apportionment formulas utilized by the standards. The only method by which this data can be collected is a special on-site study of the line in question.

As a follow-up to the Philadelphia meeting, field trips were conducted in Delaware and Ohio. The purpose of the trips was to determine the extent to which on-branch direct costs could be ascertained at the local level. It was found that by using records maintained at the local level, it is possible to ascertain direct costs related to most maintenance of way and transportation accounts. During the tests, it was possible to determine the actual number of train trips, time involved, crew costs, number of cars originated and terminated, and maintenance of way labor and supply costs for the branches involved.

As a result of the data collected on the field trips, it was possible to compute the revenues attributable and on-branch avoidable costs as defined in the standards adopted on July 1. No problems relating to computation were discovered in connection with the method by which revenues are determined under those standards. The waybill abstract data proved to be fairly accurate. The only problem identified related to timing, for the Penn Central file related to when

the waybill was abstracted rather than when the shipment occurred.

However, the same cannot be said with respect to avoidable costs. There is a lack of detailed cost data on a uniform basis. While the test group was able to identify actual on-branch costs for certain accounts, the methodology utilized would not necessarily be workable on all such tests since informal records were the source for certain accounts.

The July 1 standards provided for the use of apportionment formulas for certain accounts when direct costs are not use of apportionment formulas for certain accounts, serious inequities could result from their application. For example, an application of those apportionment formulas to the Georgetown-Lewes line would have assigned over \$44,000 for the maintenance of way accounts while the informal records indicate that there had been no actual costs incurred except

for track patrol. Similar results were obtained in the Columbus-Holmesville line. Only \$77,109 was identified on an actual basis for these accounts, while the apportionment formula would have assigned \$290,294.

Similar disparities in transportation expenses would result if the number of trips and time per trip were estimated inaccurately. While this may sound like a truism, it was found that "educated" estimates were significantly higher than the actual records indicated for these factors.

Even though a conscientious effort was made to estimate these factors on the two test lines, they were substantially overestimated in both cases. Holidays, track maintenance, equipment breakdown, or lack of traffic can result in trips canceled or shortened.

A comparison of 1973 allocated and actual on-branch costs is shown below.

	Georgetown/Lewes		Columbus/Holmesville	
	Allocated	Actual	Allocated	Actual
Maintenance of way/structures.....	\$14,806	10	\$290,294	\$77,109
Maintenance of equipment.....	4,181	\$4,181	49,806	49,806
Transportation—Rail line.....	42,903	28,799	\$79,941	320,430
Taxes, except income taxes.....	9,961	2,730	198,400	184,000
Total on-branch costs.....	100,811	30,730	\$618,441	408,228

<sup>1</sup> Excludes track patrol.

#### POSITIONS OF THE PARTIES AND DISCUSSION

Several petitions were filed requesting that the Office modify the standards. The participating parties are listed below. Other issues were raised during the public seminars and the branch line tests. A discussion of the major issues and their resolution follows:

**Concept.** The issue most often raised is the use of historical data as the basis of the subsidy payment. There is near unanimity in the position that the standards should employ actual rather than historical data, with parties representing all factions including railroads, shippers, and local, State and Federal agencies, opposing the approach taken in the standards adopted July 1. The arguments presented include illegality (i.e., prior year costs are not "avoidable costs"), unavailability of data, and various inequities to either the railroad or the subsidizer based on year-to-year cost variances. Among other disadvantages to the use of historical data cited by the parties include the lack of recognition of rate and wage increases and inflation.

Several of these problems also surfaced during the tests.

The original decision to use historical data was based upon the need for certainty in the actual amount of the subsidy payment. It was feared that potential subsidizers (principally government entities) could not enter into a subsidy agreement unless it involved a fixed amount. The New England Regional Commission (supported by six New England States) continues to argue this position.

As pointed out by the New England Regional Commission, an after-the-fact adjustment would result in a form of a cost reimbursement contract. They suggest that such an agreement may be unconstitutional in certain states. Even if it is not unconstitutional, they submit that cost reimbursement contracts provide little incentive for efficient performance and require adequate accounting systems to assure proper reimbursement.

While none of the petitioners noted the fact, it has been learned that several States have other, and possibly more significant, legal problems with the sub-

sidy program. Many States are prohibited from using public funds to subsidize a private entity. A survey reveals that most States are taking action to resolve this problem by amending the law or by channeling funds through intermediate authorities. The Office is confident that with the same ingenuity the States can resolve any cost reimbursement prohibition.

The Office also recognizes that the open-end feature is especially critical when a small community or private party is involved as the subsidizer. A substantial increase in the payment could result in serious financial problems, possibly even insolvency. This potentiality could foreclose the possibility of subsidy by smaller interests. While the Office recognizes these disadvantages, it is believed that they can be eliminated, reduced, or at least neutralized.

The Office believes that the nature and complexity of cost and revenue factors involved in subsidy agreements preclude reasonable accuracy in negotiation of an approximate fixed price. Even if service and maintenance levels could be accurately forecast, changes in the traffic level could substantially alter the subsidy payment. It is believed that the requirement of branch level data collection and written reports will provide an adequate basis for the determination of reimbursable costs.

The amended standards will place a 15 percent upward ceiling to the end-of-year adjustment, which will tend to act as an incentive to the railroad to keep costs within the estimated level. It will also provide a maximum level of payment for a given subsidy year, thus eliminating the open-end aspects of the agreement. Treating the remainder of the adjustment as a subsequent year cost will allow the railroad to recoup its legitimate reimbursement if the agreement is continued and allow the subsidizer a chance to reconsider his subsidy decision in the light of a new estimated level of payment. If the agreement is not continued, the railroad would lose the amount of the carry-over but would be relieved of the duty to continue service. Since a downward adjustment will not place a financial burden on either party, no maximum was set for refunds.

The use of actual year data would also provide an incentive to the subsidizer to increase revenue through encouragement of traffic growth. Many of the costs involved, especially maintenance of way, will not increase in direct proportion to increased traffic for the type of line involved in the subsidy program. Even if such costs do increase,

there is usually a time delay. As a result, a significant increase in revenues could substantially reduce the short run subsidy payment. It is believed that the disadvantage of utilizing historical data overrides the need for absolute certainty. Accordingly, the standards will be revised to utilize actual subsidy year data for both revenues and costs.

The handling of bridge or overhead traffic was the subject of some discussion. It was suggested that the initial standards do not go far enough in crediting the branch with its inherent advantages. The initial standards attributed all bridge or overhead traffic to the branch if termination of service on the branch would cause the railroad to lose the traffic. They also attributed potential losses in revenues resulting from rerouting of such traffic as revenue to the branch. In addition, many suggested that the additional costs incurred by a railroad in rerouting should be treated as a savings to the branch.

The use of actual year data resolves these issues. Branch or overhead traffic will be treated on the basis of actual experience. The railroad's revenues for such traffic will be prorated to the branch on the basis of miles that the bridge traffic moved on the branch to the miles the traffic moved on the system. On-branch costs for such traffic will be calculated on the same basis as traffic originated or terminated on the branch.

The decision to adopt standards that utilize actual subsidy year data leads to the requirement of developing an interim method of estimating the subsidy payment for use in deciding whether or not to subsidize and in negotiating the subsidy agreement. Several parties, including the New England Regional Commission and the Penn Central Transportation Company, suggested methods of estimating the subsidy payment. Other parties also stressed the need for a quick, easy-to-apply formula for use in the initial decision stage. The revised standards incorporate portions of each of these approaches.

Many petitioners challenged the use of apportionment formulas, especially those that relate solely to the branch. In particular, they complained that the adopted apportionment formulas for maintenance of way and transportation expenses grossly overstate the actual expenses involved. As reported in the discussion of the tests conducted by the Office, this concern was found to be especially true for maintenance of way and the crew cost portion of transportation costs. In both tests, the apportionment of these ex-

penses substantially overstated the actual situation. The adoption of a method that incorporates actual expenses will eliminate this problem.

Most of the opponents to the use of historical data and apportionment ratios also suggested that a branch line accounting and reporting system is necessary in order to obtain the required data. While it may be desirable to have such a system-wide accounting and reporting system, one cannot be justified on the basis of the subsidy program alone.

As was mentioned earlier, representatives of the railroad industry (i.e., The Association of American Railroads and the Penn Central Transportation Company) strongly urged the adoption of the standards based upon actual operation. Inherent in this approach is the ability to identify actual expenses. All railroads must have some mechanism to isolate costs if they are involved in joint-use facilities, leased lines, or passenger operations involving either a subsidy or payment from Amtrak. During the test, it was ascertained that Penn Central could easily modify its accounting procedures to collect data prospectively and thus identify on an actual basis most on-branch expenses. Staff contacts with the other railroads in bankruptcy indicated this to be true for them as well. As a result, the revised standards will require railroads to collect actual data for certain accounts covering branch lines involved in subsidy agreements. The data collection would be limited to the period of the subsidy and to accounts related to the specific branch.

Section 304 of the Act provides that all rail services may be discontinued, and the underlying rail properties abandoned, if they are not included in the final system plan, unless a shipper, a State, the United States, a local or regional transportation authority, or any responsible person offers to subsidize the service or purchase the properties. In the situation where a new rail service continuation subsidy is offered to preclude discontinuance or abandonment, the amount must cover the difference between the revenue attributable to such rail properties and the avoidable costs of providing service on such rail properties plus a reasonable return on the value of such rail properties. The standards promulgated herein define those terms and, as a result, provide a basis for calculation of the subsidy payment. Since the U.S. Railway Association is not required to utilize these standards as criteria for inclusion of branch lines in the Final System Plan, there is a distinct

possibility that a branch could be excluded from the plan yet be profitable under the standards. It is obvious from a reading of the Act that branches caught in such a circumstance should be protected from discontinuance of service. Therefore, to assure that such a circumstance does not arise, the Office establishes the amount a potential subsidizer must offer under section 304(c)(2)(A) of the Act as the amount computed in accordance with the interim formula, or \$1 whichever is the greater amount.

**Interim subsidy payment.** The amended standards at § 1125.3, include an interim formula to be used as the basis for computing the initial subsidy payment and for negotiating the subsidy agreement. The parties will be free to negotiate on almost all agreement provisions; however, standards are established which can be invoked in case of impasse.

To assure consistency with the reorganization process decisions, the interim formula will be based on the same year data that the U.S. Railway Association employs in its decision-making process. At the present time it is assumed that the light density line viability decisions will be based upon 1973 data, primarily the 1973 waybill abstract files. It was found during the branch line tests that these data are reasonably accurate.

An advantage to the use of these data will be the assistance the Office can give to the parties. While the railroads will be required to file comprehensive revenue and cost data along with their notice of intent to discontinue service, the Office can accelerate the process by making much of the data available in advance to those that wish to have it. Timing is a critical factor since the Act provides a potential subsidizer only 60 days from the date a railroad files a notice of intent in which to decide whether or not to offer a subsidy and thereby preclude discontinuance of service.

Information needed to calculate the interim formula can be divided into four primary categories: revenues, off-branch costs, on-branch costs, and value of rail property.

Using the waybill abstract files as a data base, the Office will be able to make freight revenue and off-branch cost calculations available to interested parties. While the interim formula will take other sources of revenue into consideration, in most instances, freight revenues will represent the only significant source of income for the branch line.

Off-branch cost calculations relate



solely to freight traffic. With these two factors available in advance, and with assistance from the Office available upon request to aid in developing the remaining factors, it is believed that the timing problem can be reduced substantially. The following standards will be utilized in the interim formula unless the parties agree on different levels.

The estimate for "revenues attributable" will include the same sources of revenues as those required in the standards. These include freight and passenger revenues from all traffic originated or terminated on the branch, existing subsidy payments, overhead traffic and accessorial revenues. All of the data will be presented for the same base year as employed by the Association in the decision-making process (presumably 1973). These data may be adjusted for rate changes. By agreement of the parties, more current figures may be used.

A ratio of the off-branch costs to revenues for the base year will be calculated for each branch. The ratio will be applied to the estimated revenue for the subsidy year to determine the estimated off-branch cost. The off-branch calculation will utilize variable system average costs, short line mileages, and traffic information from the waybill abstract files. The Office will computerize the formula and make the calculations available to interested parties.

On-branch costs will be divided into six categories: Routine maintenance of way and structures, rehabilitation, maintenance of equipment, transportation, miscellaneous, and taxes. A minimum level of maintenance of way and structures is prescribed. The branch line tests revealed that the type of track involved in the subsidy program will have been subjected to various levels of deferred maintenance. The interim formula establishes the Federal Railroad Administration's (FRA) safety standards for Class I track as the minimum allowable track condition. FRA requires periodic inspection of track depending upon the class and use of the track. The expenses involved in inspection, vegetation control and spot or emergency maintenance to meet minimum Class I track standards must be included in the calculations.

Since there will be an adjustment for actual costs, the Office believes that an arbitrary level can be utilized for estimation purposes. The inclusion of such an estimate will assure that both parties recognize their respective responsibilities. Based upon the experience gained in the branch line tests, it would appear

that such maintenance can be performed for approximately \$1,000 per mile per year. Both lines tested fell into a minimum maintenance category. The Georgetown-Lewes line had no maintenance costs other than track patrol, and the Columbus-Holmesville line averaged approximately \$1,000 per mile.

This, of course, does not cover any so-called "programmed maintenance" or rehabilitation costs. If, at the time the notice of intent is filed, the track does not meet FRA Class I standards, it will be mandatory that such rehabilitation costs be covered by the subsidy. In such cases the railroad will be required to furnish a detailed estimate of the costs to rehabilitate the track to Class I standards with the notice of intent to discontinue service.

The Office also recognizes that under some circumstances, even though the track will meet minimum standards, this level of maintenance will not be satisfactory. Higher levels may be negotiated by the parties in such cases. As mentioned above, the incentive to reduce transportation costs should encourage upgrading of track conditions where normal speed limits are impaired.

The estimate for maintenance of equipment will be based upon an application of system average costs per locomotive gross ton-mile for road locomotive repairs and locomotive unit-hours for yard locomotive repairs. Locomotive depreciation also will be based on locomotive unit-hours. Passenger car depreciation will be based upon a passenger car-mile ratio. Freight car costs will be based upon an average per day and per mile car cost. The railroad will be required to furnish an estimated number of days a freight car will remain on the branch.

Transportation costs will be estimated based upon system average costs. The number of trips per year will be based upon the frequency of service performed at the time the notice is filed unless the parties agree to a different level. Labor costs for train crews will be based on system average costs for each type of crew applied to the hours of service on the branch. Fuel costs will be based upon system average costs per locomotive unit-hour and train supplies and expenses on average costs per train-hour. This information will be furnished by the railroad with the notice of intent. The railroad will also furnish estimates of costs for the remaining transportation accounts using the final standards as a guide to their inclusion.

The estimate for miscellaneous expenses will include only those direct out-

lays anticipated during the subsidy year. The railroad will be required to furnish an estimate with the notice of intent.

The estimate for property taxes will be based upon the base year actual, adjusted for tax rate changes. Revenue taxes will be based upon the revenue level estimated by the interim formula. The remaining factor, value of property, will be estimated by the railroad when the notice of intent is filed. The basis of the valuation will be the net liquidation value for non-rail transportation purposes of the rail properties used or useful in performing the service. If the valuation is challenged an appraisal of the property by a qualified and certified appraiser or appraisers may be offered by the potential subsidizer. If the parties cannot agree on a valuation through negotiation an average of the two appraisals will be used as the basis of the interim formula and the final value will be determined through arbitration before the end of the first subsidy year.

The present standards, as modified herein, will provide the basis for the actual subsidy payment. The standards will provide for a final payment adjusted for actual experience during the subsidy year. Railroads involved will be required to establish a system of collecting costs and other relevant data at the branch level and to provide the subsidizer with periodic financial reports which analyze the actual data in relation to the estimates. Significant deviations from the estimates will have to be explained in the report. Increases over 15 percent in the amount of actual subsidy payment as compared to the estimate will be treated as a carry-over cost in the subsequent year.

**Revenues.** The regulations relating to revenues are to be found in § 1125.4 of the revised standards. The Association of American Railroads, United States Department of Transportation, and others suggest that freight revenues be prorated on a mileage ratio between the branch and the system, and consequently, that off-branch revenues and costs be eliminated from the standards. The Office believes that this approach would not fairly represent the revenues a branch contributes to the system. Since there appears to be no accepted method of dividing revenues, the Office believes that the adopted standards provide the most equitable approach.

The Commonwealth of Pennsylvania suggested the use of a passenger ratio and the Association of American Railroads suggested the use of a passenger car-mile ratio rather than the adopted passenger-mile ratio to determine pas-

senger revenues. A passenger ratio does not take into account the distance factor and a passenger car-mile ratio does not relate to revenues derived. Therefore, it is believed that the passenger-mile ratio adopted in the original standards should be retained.

**Avoidable costs.** The cost standards, contained in § 1125.4 of the regulations adopted July 1, appear as § 1125.5 of the revised standards. The majority of the comments were directed toward the standards for determining avoidable costs. The problems involving the use of historical data, apportionment, and data availability have been treated above.

The widest range of disagreement between the petitioners arises in the discussion concerning the cost accounts to be included in the standards. Basically, the parties representing railroad interests support full allocation of all costs. The potential subsidizers takes the position that the standards should exclude indirect costs.

The Office agrees that the phrase "avoidable cost" should be strictly construed, but this fact does not necessarily exclude indirect costs. It is important to note that the Act discusses avoidable costs in the context of *providing* the service not of *abandoning* the service. This distinction is significant. Equipment depreciation accounts best illustrate this distinction. As many parties suggest, capital investment is a "sunk cost" and the depreciation thereof, taken from the viewpoint of abandonment, is not an avoidable cost. However, when viewed from the standpoint of a continuing operation, capital investments in equipment must be made from time to time in order to maintain service; and, consequently, depreciation costs for these items would be avoidable. The same principle would also apply to structure depreciation, but, the standards provide that rehabilitation costs be recovered during the period covered by the subsidy agreement. In effect, capital investment in structures is treated as an expense. Each on-branch account has been reviewed and the modifications reflected in the amended standards are summarized below.

**Account 266—Road property—depreciation.** This account will be deleted from the standards. Investments made prior to the subsidy agreement represent "sunk" costs. Future investments in this type of property will be treated as current expenses under the provision covering adequate and efficient rail service.

**Account 267—Retirements; and Account 270—Dismantling retired property.** These accounts will be deleted from the standards entirely since they do not re-



late to the costs of providing service.

**Account 542—Rent for leased roads and equipment.** This account will be deleted from the standards since any costs involved are included in the return on investment.

The following accounts will still be included; however, the basis of their assignment to the branch has been altered or they have been grouped with other accounts.

**Account 311—Locomotive repairs.** This account will be separated between yard and other (road) and each in turn will be separated between diesel and other (electric). The service unit factor for yard locomotives shall be the ratio of locomotive unit hours separated between diesel and electric on the branch to those of the total system. The service unit factor for other (road) locomotives shall be the ratio of locomotive gross ton miles on the branch separated between diesel and electric to those of the total system.

**Account 314—Freight train car repairs.** On-branch car costs shall be calculated on the basis of system average day and mileage ratios. This account will be one element in the car cost per day and per mile calculation.

**Account 330—Equipment retirements.** The only amounts includable shall be for specialized equipment that would be expendable as a result of abandonment, such as floating equipment 330(56).

**Account 372—Dispatching trains; Account 373—Station employees; Account 374—Weighing, inspection, and demurrage bureaus; Account 375—Coal and ore wharves; Account 377—Yardmasters and yard clerks; Account 379—Yard switch and signal tenders; and Account 407—Communication system operation.** The costs assigned under these accounts shall be the actual branch costs assigned on a direct basis and will be assignable only if it can be demonstrated that such costs would be avoided as a result of the service being discontinued.

**Account 376—Station supplies and expenses; and Account 389—Yard supplies and expenses.** The costs assigned under these accounts shall be the actual branch costs assigned on a direct basis.

**Account 378—Yard conductors and brakemen; and Account 380—Yard enginemen.** These costs shall be assigned only on a direct basis.

**Account 382—Yard switching fuel.** This account shall only be includable when the branch is served by diesel locomotives classified as a yard switch engine. The service unit factor shall be the ratio of diesel locomotive unit hours-yard, on the branch to those of the total system.

**Account 383—Yard switching power produced; and Account 384—Yard switching power purchased.** These accounts shall only be includable when electric locomotives classed as switch engines are used to serve the branch. The service unit factor shall be the ratio of electric locomotive unit hours on the branch to those of the total system.

**Account 388—Servicing yard locomotives.** This account shall only be includable when the branch is served by locomotives which are classed as switch engines. The service unit factor shall be the ratio of yard locomotive unit hours on the branch to those of the total system.

**Account 392—Train enginemen; Account 401—Trainmen.** These costs shall be assigned only on a direct basis.

**Account 394—Train fuel.** This account is only to be included when service on the branch is performed by diesel locomotives in local/way or through train service. The service unit factor shall be the ratio of diesel locomotive unit hours on the branch to those of the total system.

**Account 395—Train power produced; and Account 396—Train power purchased.** These accounts shall only be includable when electric locomotives in local/way or through train service are used to serve the branch. The service unit factor shall be the ratio of electric locomotive unit-hours on the branch to those of the total system.

**Account 400—Servicing train locomotives.** This account shall be apportioned to the branch on the basis of the locomotive unit-miles on the branch to those of the total system.

**Account 404—Signal and interlocker operation; and Account 405—Crossing protection.** These accounts shall be included on an actual basis only.

**Account 503 Cr.; and Account 536 Dr.—Hire of freight cars and highway revenue equipment.** On-branch car costs shall be calculated on the basis of system average day and mileage ratios. The freight car portion of these accounts shall be elements in the calculation of car cost per day and per mile. The highway revenue equipment would only be allowed on a direct basis.

**Accounts 277, 335, 409, and 449—Employees health and welfare benefits; and Payroll taxes.** These costs shall be included in the subsidy calculations on a basis that will allow for a reasonable assignment of these costs in proportion to the labor costs incurred.

The following accounts will be added to the standards:

**Account 331—Equipment-Depreciation.** (52) Locomotives—Yard. This account

shall be included if the branch is served by yard locomotives. The cost shall be assigned to the branch based on the ratio of the locomotive unit-hours on the branch to those of the total system.

(52) **Locomotives—Other.** When a branch is served by a local/way or through train crew the expense shall be assigned to the branch on the ratio of locomotive unit-hours on the branch to those of the total system.

(53) **Freight-train cars.** On-branch car costs shall be calculated on the basis of system average day and mileage ratios. This is an element in the cost per car day and per car-mile calculation.

(54) **Passenger-train cars.** In those instances where passenger service is offered on the branch, this expense shall be assigned on the basis of the passenger car miles on the branch to those of the total system.

(55) **Highway revenue equipment.** Only equipment which is specialized in its capacity and/or would not be used elsewhere in revenue service may be included. The inclusion of the expense shall be on an actual basis only.

(56) **Floating equipment.** Expenses relating to equipment under this category for which there would be no further need shall be included on an actual basis only. Equipment depreciation costs must be treated as an avoidable cost in recognition of the requirement for equipment replacement.

**Account 505—Rent from passenger-train cars; and Account 538—Rent for passenger-train cars.** Those branches having passenger service shall include these accounts in those instances where the rental of specific equipment will cease upon the termination of operation on that particular branch.

**Freight-train car costs.** The on-branch costs for time-mileage freight-train cars shall be calculated on the basis of applying the railroad's average costs per car-day and per car-mile to the actual number of car-days and car-miles accumulated on the branch during the subsidy year. These costs shall include Account 314—Freight-train car-Repairs; Account 331(53) Equipment-Depreciation of Freight-train cars; freight car portion of Account 503—Hire of freight cars and highway revenue equipment—credit; freight car portion of Account 536—Hire of freight cars and highway revenue equipment—debit; and the return on investment in freight-train cars.

The system totals for repairs and depreciation shall be divided into time related and mileage related costs on the basis of the standard Rail Form A apportionment factors (i.e., 50 percent time

and 50 percent mileage for repairs and 60 percent time and 40 percent mileage for depreciation). Return on investment shall be treated as a 100 percent time-related cost. The system total receipts and payments for the hire of time-mileage cars and the basic data used in the development of the car-day and car-mile factors shall be taken from the railroad's latest Form R-1.

The on-branch costs of freight cars rented on a straight mileage basis shall be the system average cost per mile applied to the total miles accumulated on the branch loaded and empty. The data necessary to calculate the mileage costs shall be taken from the Form R-1.

Some parties challenged the use of the functional service unit costs developed by the application of Rail Form A, as the basis of determining off-branch costs since it utilizes variable costs. They suggest that Rail Form A was not designed to develop avoidable costs and that its use for that purpose is improper. While on the surface it might seem inconsistent to allow system variable costs to be allowed for off-branch costs, it is believed justified on the basis of equity to the railroad since all system revenues from traffic originating or terminating on the branch are attributed to the branch. A failure to recognize off-branch variable costs would probably lead to situations where the operating railroad would try to divert the traffic to another carrier at the earliest possible point regardless of service considerations. This would not only result in circuitous movement and concomitant time delays but would also decrease the revenue attributable to the branch. The adopted approach recognizes the services rendered by the carrier to the branch traffic.

It was also suggested that the use of Rail Form A results in double counting of certain terminal handling costs. As a result of these suggestions, the use of Rail Form A was reviewed and it was determined that certain modifications were desirable.

The off-branch costs can be separated into two distinct categories; terminal and/or interchange costs, and line-haul costs. The initial standards provided that the terminal cost be taken directly from an application of the carrier's Rail Form A. The terminal costs basically consist of three categories of expense: switching costs, car ownership costs, and station billing and other clerical costs. It has been correctly suggested that certain elements of the terminal cost at the branch end of the movement are duplicated through the on-branch costs. The revised standards will eliminate these

elements. "Intertrain switching" costs shall be substituted for the "road train to industry" switching costs currently used in the calculation. The car ownership portion of the terminal cost shall be modified to employ the same concept used in the on-branch car cost (i.e., cost per car-day). Two days will be allowed in the terminal area at the branch end of the movement to cover both the loaded and the empty car moves. The third category of expense, the station billing and other clerical costs, shall remain the same unless the station billing function is actually performed on the branch. In such cases, these costs shall be omitted from the off-branch calculation and included as a direct on-branch cost.

The method of providing for costs relating to rehabilitation and/or upgraded service gave rise to several comments. The parties representing potential operating railroads support the proposition of total "front-end" loading of such costs while the potential subsidizers favor spreading the costs over a period of years. In certain cases the front-end loading of these costs will undoubtedly create monetary hardships on the subsidizer. While the fact that Federal matching funds are authorized for only two years cannot be ignored, there is nothing to preclude long-term subsidy agreements. The modifications to the standards will assure considerable flexibility between the parties to the subsidy agreement, including the ability to spread such costs over a longer period. This would be especially true where a subsidy is offered that does not involve Federal funds.

Many parties also suggest that the subsidizer should obtain an interest in the rehabilitated property. This argument has merit only if the rehabilitation increases the net liquidation value of the property. The subsidy agreement could include a provision to cover this possibility.

It may be true, as many parties suggest, that where substantial rehabilitation costs are involved, a potential subsidizer might protect his investment more effectively by purchasing the line.

Since the parties are given considerable latitude in establishing service and rehabilitation levels through the interim formula, the necessity for the subsection (formerly § 1125.4(1)) covering adequate and efficient rail service has been eliminated.

*Investment base and reasonable return on the value:* Comments relating to the "reasonable return on the value" were directed toward two primary areas, valuation and rate of return. Some parties

challenged the authority of the Office to issue standards for determining the value of the rail property involved. However, as already noted, section 205(d) of the Act places the responsibility upon the Office for determining the meaning of certain phrases used in section 304, including a "reasonable return on the value" of rail properties over which subsidized rail service is to be performed. The Office believes that a reading of these two sections together makes clear the Congressional intent that the standards provide a formula by which a monetary sum (subsidy payment) may be readily computed. It is impossible to develop a meaningful formula for this purpose without determining standards for valuation of the properties to which the reasonable rate of return is to apply.

A few parties questioned use of the term "net liquidation value" for determining the investment base to which the reasonable return is to apply. Some suggested use of the term "salvage value" as employed by the Commission in abandonment proceedings; others, such terms as "original cost less accrued depreciation" sometimes employed by regulatory agencies in rate-making proceedings; and still others the terms "market value" or "fair market value."

It should be pointed out that section 304 contemplates a situation wherein a railroad has transferred to Consolidated Rail Corporation or to other railroads all or substantially all of its rail properties designated for such conveyance in the final system plan. It is thereupon relieved of its common carrier obligations, and rail service on the remainder of its rail properties may be discontinued and these properties abandoned pursuant to section 304(c) notwithstanding any provision of the Interstate Commerce Act, the constitution or law of any State, or the decision of any court or administrative agency of the United States or of any State unless a rail service continuation subsidy is offered. Thus, the circumstances are not analogous to those involved either in an abandonment proceeding under section 1(18) of the Interstate Commerce Act or in the determination of a reasonable return on an investment base necessary for the continuing discharge of common carrier obligations in the public interest. In the usual case the owners of the properties being considered for subsidy under this section will be the trustees of a railroad in reorganization or their successors in interest. It should be noted also that the valuation standards promulgated herein do not apply to an offer to purchase pursuant to section 304(d).

Some parties urged that it is unreasonable to limit the value of the properties to their highest and best use for purposes other than rail transportation. This limitation was imposed initially under the theory that a notice of intent to discontinue service necessarily would indicate a belief of the owners that the highest and best use of the property would not be for common carrier rail transportation purposes.

It is conceivable that a governmental authority or other responsible persons might wish to purchase a property on which the owners propose to discontinue service, expecting to operate it as a subsidized short line railroad. Or, the trustees or owners of a particular property subject to section 304 might, if a subsidy were available, decide to continue operations rather than abandon. In either of these cases, there appears to be no justification for inserting in the subsidy formula a return on an investment base greater than that which would have motivated the trustees or owners to decide upon abandonment in the absence of subsidy. That base would be the net liquidation value for purposes other than rail transportation. Consequently, the limitation will remain in the standards.

Most of those commenting agree that some sort of arbitration procedure would be necessary in the event of disagreement between the parties as to the properties that are used or useful or the net liquidation value. Some have argued that the arbitration should not be final or binding. The Office does not perceive that the arbitration would serve any useful purpose if not final and binding. Further, it is implicit in sections 205(d)(3) and 304(c) that the determination of subsidy standards by the Office was intended by Congress to be final and binding. It follows that arbitration of any differences as to the meaning of these standards should also be final and binding. It is noteworthy that none of the comments took issue with the proposed procedure for naming arbitrators.

Some of the comments argued that "opportunity costs of capital" for most railroads are higher than the rate of return set by the standards. This may be, although no persuasive evidence to this effect was presented. In any event, the standards do not apply to "most railroads," but only to those which would be relieved of common carrier obligations under section 304 of the Act.

For similar reasons, the reasonable rate of return is not necessarily one which, taking account of the risks and

hazards incident to common carrier rail transportation, would permit the trustees or managements of railroads to attract capital to enable continued rail transportation operations responsive to the public needs. Were these trustees or managers in charge of an on-going, profitable transportation concern, they might choose to invest the proceeds of an abandonment in improving the remainder of the rail properties in their care, considering that course to be in the best interests of the investors for whom they are fiduciaries. In the circumstances contemplated by section 304 of the Act this is unlikely, and an external investment appears to furnish a more likely measure of their fiduciary opportunities. Also, the reasonable return under consideration in § 1125.7 applies to prudent investment of funds gained from partial recovery of previously "sunk" capital, rather than commitment of such funds to new ventures.

Should the return allowed be too small, it would not satisfy minimum constitutional standards of sufficiency; moreover, achievement of the overall goals of the Act would seem to require that consideration be given to reasonable treatment of investors in the profitable railroads and those in reorganization within the region. Also, investors as a class (holders of interests in insurance policies, savings accounts, pension plans, etc.) constitute a wide segment of the public whose interest the Act is designed to serve. But if the return allowed is unreasonably high in the light of the applicable circumstances, an unfair burden would be placed on the subsidizing body.

Some of the comments have suggested a fixed rate of return, such as 10 percent after income taxes. The Office considers that the standard for rate of return ought not only to be as simple and readily determinable as possible, because it will apply at some time in the future in which prevailing capital market conditions cannot be predicted with certainty, it also should be flexible. Consequently, the concept of a fixed rate of return is rejected.

Some of the comments received argue that the return should be computed after allowance for income taxes, urging that for most taxpaying railroads the tax shield is one of the most important economic values involved in an abandonment decision, and in one instance citing the hypothetical example of a railroad with a marginal tax rate of 50 percent. The Office has been unable to locate any example of a railroad in the region enjoying an effective income tax rate at this level.



In any event, we are concerned here not with "most taxpaying railroads," but primarily with those rail properties of bankrupt carriers not designated for rail service operations in the final system plan and as to which service discontinuance notices have been given as specified in section 304(a). The Office is aware that income tax considerations are customarily given weight by regulatory authorities in determining the rate of return necessary to sustain on-going public service operations. For reasons previously outlined, however, these considerations do not apply in circumstances envisaged by section 304. Where trustees of a railroad in reorganization or a profitable railroad in the region which has transferred substantially all of its rail properties to Consolidated Rail Corporation or other railroads pursuant to the final system plan actually to abandon the remaining rail properties, the proceeds of such abandonments would have to be prudently invested or paid out to investors or claimants for which the trustees or managers of these railroads are fiduciaries. What income tax rates would apply to the earnings from such investments or to such payouts cannot presently be foreseen, but the applicable taxes would be the obligation of the trustees, the profitable railroad, or those who receive the payouts, as the Internal Revenue Code might provide. Thus, to require those who provide a subsidy for continuance of rail services to include in their payments any pre-determined allowance for taxes over and above the pre-tax return which could be obtained on the proceeds from abandonment does not appear to be warranted.

The Penn Central trustees point out certain difficulties with the language of § 1125.6 of the standards published July 1 (§ 1125.7 of the revised standards) and also urge that, to avoid limiting subsidy agreements to seven years or less, Treasury bonds as well as notes be included in the securities employed to measure reasonable return on the value. Some issues of Treasury bonds, in contrast to notes, may be called for redemption, at the option of the United States, prior to maturity. Also, certain series of Treasury bonds no longer issued but still outstanding in quantity, may be redeemed at par and accrued interest prior to call or maturity for the sole purpose of paying Federal estate taxes due from the estate of a deceased owner. One non-marketable series is exchangeable for marketable 1½ percent Treasury notes of series EA or EO. These should be excluded from the definition of obligations to be considered in determining the return.

Amended § 1125.7 has been revised to take account of these suggestions, and to exclude Treasury bills, which have a life of less than one year.

The Penn Central trustees also comment that, although the Act provides for limited Federal assistance to the subsidizing bodies, this is not tantamount to a guaranty of the subsidy agreements. Accordingly, they urge that the owner of the line at least receive a premium of 20 percent over the specified rate; 10 percent being assignable to risk and the other 10 percent to the lack of liquidity of the investment.

While it is true that the subsidizer may have a credit standing inferior to that of the United States and that the subsidy agreements may not be as liquid as Treasury obligations, it is believed that the difficulties involved in quantifying these factors negate their application.

The difficulty here is that the trustees do not present any specific rationale to justify the 20 percent, or any other fixed premium. Certainly, it could not properly be applied in a case where the United States was the subsidizing body.

The Office has endeavored to develop some ready mechanism by which the relative credit standing of each subsidizing entity could be factored into the rate of return. One approach considered was to hinge the rate of return upon a rating assigned by the standard rating services, such as Moody's Standard and Poor's or Fitch. Over the ten years 1964-1973, for example, average yields on Moody's Aaa industrial bonds were 10.8 percent below the average for Baa industrials, and average yields on Aaa municipals were 6.3 percent less than the average for Baa municipals. However, these ratings apply to particular bonds, not to the issuers of them. In practice, many of the subsidizing bodies may not, at the time of entering into a subsidy agreement, have any outstanding securities held by the public, and thus may have no ratings from any of the accepted rating services.

Consideration also was given to establishing some other measure of return than Treasury obligations as possibly more nearly reflecting the relative risk. Inquiry of the rating services failed to disclose any publicly quoted, regular, periodic listing of yields on industrial and municipal securities which would be legal for investment by fiduciaries. The Office, therefore, believing that in view of time constraints the need for a readily measurable and publicly available standard is overriding, considers that the use of United States Treasury obligations for this purpose, without any arbitrary pre-

mium, will yield the maximum degree of fairness to all parties.

#### PARTIES FILING PETITIONS

##### GOVERNMENT

###### Federal

Office of Public Counsel, Rail Services Planning Office  
United States Department of Agriculture  
United States Department of Transportation  
United States Railway Association

###### State

Commonwealth of Massachusetts, Office of Transportation and Construction  
Commonwealth of Pennsylvania  
Commonwealth of Pennsylvania Department of Transportation  
New York State Department of Transportation  
Office of the Governor of West Virginia  
Pennsylvania Public Utility Commission and the Pennsylvania State Legislative Board, United Transportation Union (jointly)  
State of Connecticut Department of Transportation  
State of New Hampshire  
State of New Jersey Department of Transportation  
State of Rhode Island and Providence Plantations Department of Transportation  
State of Vermont

###### Local

Chester County Planning Commission  
City of Philadelphia  
Council on the Environment of New York City

###### Regional

Appalachian Regional Commission  
New England Regional Commission

###### Business

Agrico Chemical Company  
Air Products and Chemicals, Inc.  
Armstrong Cork Company  
Archer Daniels Midland Company  
Borden Chemical  
E. Keeler Company  
Evans Products Company  
FS Services, Inc.  
Hammermill Paper Company  
Illinois Grain Corporation  
Imperial Oil Company  
Institutional Investors Penn Central Group and Certain Indenture Trustees  
International Minerals & Chemical Corporation  
PPG Industries, Inc.  
Royster Company  
Sperry New Holland  
Swift Chemical Company  
Trans-Act Association, Inc.

###### ORGANIZATIONS

Adrian Area Chamber of Commerce  
National Industrial Traffic Leagues  
New Jersey State Chamber of Commerce

#### RAILROADS

Association of American Railroads  
Detroit, Toledo & Ironton Railroad Company  
and The Ann Arbor Railroad Company  
Central Railroad Company of New Jersey  
Penn Central Transportation Company  
Southern Pacific Transportation Company

#### CONCERNED CITIZENS

Allan J. Barnes  
Thomas Park Shearer

#### ORDER

In consideration of the foregoing: *It is ordered*, That Part 1125 of Subchapter B of Chapter X of Title 49 of the Code of Federal Regulations, be amended by substituting standards set forth below, for the standards adopted on July 1, 1974.

*It is further ordered*, That this order shall become effective on January 8, 1975.

[SEAL]

ROBERT L. OSWALD,<sup>1</sup>  
Secretary.

Sec.	Purpose and scope.
1125.1	Purpose and scope.
1125.2	Definitions.
1125.3	Interim subsidy payment.
1125.4	Revenue attributable to the rail properties.
1125.5	Avoidable costs of providing service.
1125.6	Valuation of rail properties.
1125.7	Reasonable return on the value of the properties.
1125.8	Submission of information by railroad giving notice of intent to discontinue service on a branch.

Appendices I & II Information to be furnished.

AUTHORITY: Sec. 205(d)(3), Regional Rail Reorganization Act of 1973, Pub. L. 92-236, 87 Stat. 985, 994.

#### § 1125.1 Purpose and scope.

(a) Section 304(c)(2) of the Act provides that no rail service may be discontinued and no rail properties may be abandoned pursuant to that section if a shipper, a State, the United States, a local or regional transportation authority, or any responsible person offers a rail service continuation subsidy which covers the difference between the revenue attributable to such rail properties and the avoidable costs of providing service on such rail properties, plus a reasonable return on the value of such properties.

(b) Section 205(d)(3) of the Act directs the Rail Services Planning Office to determine and publish standards for determining the "revenue attributable to

<sup>1</sup> Present: George M. Chandler, Director, Rail Services Planning Office to whom the matter under consideration in this docket has been assigned.



the rail properties", the "avoidable costs of providing service", and "a reasonable return on the value" as those phrases are used in section 304 of the Act. This Part sets forth those standards.

(c) The standards set forth herein employ an interim formula for establishing an estimated first year subsidy payment. This estimate will serve as a basis for the subsidy offer within the context of section 304(c)(2) of the Act and provide a framework for the negotiation of a subsidy agreement. The amount a subsidizer must offer under section 304(c)(2)(A) is the amount computed in accordance with the interim formula, or \$1, whichever is the greater amount. The final payment will be adjusted based on data related to the subsidy period. Where an adjustment results in an increase in the estimated subsidy payment, the amount of such increase in excess of 15 percent of the estimated payment shall be treated as a carry-over avoidable cost in the subsequent subsidy year.

#### § 1125.2 Definitions.

Unless otherwise required by the context, the following definitions apply in this part:

"Account" means an account in the Commission's Uniform System of Accounts for Railroad Companies (49 CFR Part 1201).

"Act" means the Regional Rail Reorganization Act of 1973, Public Law 93-236 (87 Stat. 985).

"Base year" means the same year employed by the U.S. Railway Association in developing the final system plan.

"Branch" means a segment of a railroad that is not designated to be in the final system plan under the Act, and that is the subject of a notice in writing of intent to discontinue service under section 304(a) of the Act and notice of intent to abandon rail properties under section 304(b) of the Act.

"Commission" means the Interstate Commerce Commission.

"Form R-1" means the railroad's annual report filed with the Commission in accordance with the requirements of section 20 of the Interstate Commerce Act.

"Notice of Intent" means a notice in writing of intent to discontinue service under section 304(a) of the Act and notice of intent to abandon rail properties under section 304(b) of the Act.

"Office" means the Rail Services Planning Office established by section 205 of the Act.

"Person offering a subsidy" means a shipper, a State, the United States, a

local or regional transportation authority, or any responsible person offering a rail service continuation subsidy under section 304(c)(2)(A) of the Act.

"Rail Form A" means the Commission's *Formula for Use in Determining Rail Freight Service Costs, Statement IFI-73*.

"Railroad" means a railroad company, or the trustee or trustees of a railroad company, that gives a notice in writing of intent to discontinue service under section 304(a) of the Act, and, as the context requires, "railroad" may mean either the owner of rail properties over which subsidized service is or may be performed, or the operator of that service, or both.

"Subsidy year" means any 12 month period for which a subsidy agreement is negotiated and in operation.

#### § 1125.3 Interim subsidy payment.

The person offering a subsidy shall offer to pay, in return for the continuation of rail service, an amount computed on the basis of the interim formula described in this section. The interim payment may be adjusted, by agreement of the parties, to take into account factors, such as rate increases and changes in traffic levels which would make the sole use of base year data an inappropriate means of estimating the payment for the subsidy year. The interim formula makes use of estimates of revenues, off-branch costs, on-branch costs and a return on the value of the properties involved. The "base year" for all estimates under this section shall be the same year employed by the United States Railway Association in developing the final system plan pursuant to sections 206 and 207 of the Act.

(a) *Revenues*. The estimated revenues shall include all the sources of revenue described in § 1125.4, computed on the basis of base year data.

(b) *Off-branch costs*. A ratio of off-branch costs to revenues for the base year shall be used to derive the estimate of the off-branch costs for the subsidy year. The base year off-branch costs shall be calculated using the methodology described in § 1125.5(k). If data identifying actual carloads by car type are not available, car type shall be based upon the railroad's best estimate. A ratio shall be developed by applying these costs against the base year revenues. The resulting ratio shall be applied to the revenues estimated in paragraph (a) of this section to develop the estimated off-branch cost for the subsidy year.

(c) *On-branch costs*. The estimate for on-branch costs shall be separated into the following six categories: Routine maintenance of way and structures, rehabilitation, maintenance of equipment, transportation, taxes, and miscellaneous.

(1) The costs for routine maintenance of way and structures shall be estimated at \$1,000 per year per mile of track on the branch for which the railroad is responsible for maintenance, unless the parties agree to a higher level.

(2) Rehabilitation costs will not be included unless (A) the track involved does not meet minimum Federal Railroad Administration (FRA) Class 1 safety standards (49 CFR 213), in which case, the railroad will furnish a detailed estimate of the costs to rehabilitate the track to the minimum level with the notice of intent and provision to cover such costs shall be included in the subsidy agreement; or (B) the potential subsidizer requests a level of service which requires expenditures for rehabilitation, and makes such a request within 10 days after the date the notice of intent is filed, in which case the railroad shall furnish an estimate of the costs involved within 20 days after the date of that request. All such requests and estimates shall be on a specific project basis.

(3) The estimate for maintenance of equipment costs shall be based on the same methodology employed in § 1125.5(b), using base year data rather than subsidy year data. Unless the parties agree to a different base, the resulting average unit costs shall be applied to the branch base year service units to arrive at the estimate.

(4) Transportation costs shall be estimated, based upon system average costs. The number of trips per year shall be based upon the frequency of service performed at the time the notice is filed unless the parties agree to a different level. Labor costs for train crews shall be based on system average costs for each type of crew applied to the hours of service on the branch. The crew costs shall be classified into four major categories: Yard, local/way, through, and passenger. The straight time average cost per hour for each yard or local/way crew member shall be calculated using the railroad's Employees, Service, and Compensation Report (Form B) for the base year. The calculation is made by adding together the straight time compensation, col. (9), and the constructive allowances, col. (11), and dividing this total by the straight time hours actually worked, col. (4). This process would be repeated for each yard and local/way class of employee. After the hourly rate is deter-

mined for each member, the cost per crew hour shall be calculated based on the exact size and consist of the crew currently serving the branch. The crew cost per hour is multiplied by the estimated hours that will be incurred in serving the branch during the subsidy period. If the branch is served by a through train crew, the cost shall be assigned to the branch based on the estimated train-hours that will be incurred serving the branch times the system average crew cost per freight train-hour. The crew cost per train-hour is developed by dividing the freight portions of accounts 392 and 401 (R-1, Sch. 320, col. (e)) by the train hours in freight service (R-1, Sch. 531, line 30, col. (b)). Passenger crew cost shall be based on the estimated passenger train-hours that will occur on the branch during the subsidy period times the average crew cost per passenger train-hour. The crew cost per train-hour is developed by dividing the passenger portion of accounts 372 and 401 (R-1, Sch. 320, col. (h)) by the train-hours in passenger service (R-1, Sch. 531, line 30, col. (c)). The estimated direct crew costs must be increased to cover fringe benefits using the procedure described in § 1125.5(e). The railroad shall also furnish estimates of costs for the remaining transportation accounts using the final standards as a guide to their includability and basis of calculation.

(5) The estimate for property taxes shall be based upon the base year actual tax assessment, adjusted for tax rate changes. Revenue taxes shall be based upon the revenue level estimated pursuant to paragraph (a) of this section.

(6) The estimate for miscellaneous expenses shall include only those direct outlays anticipated during the subsidy year.

(d) *Return on value*. The railroad shall appraise the value of the property on the basis of definition found in § 1125.6. If the valuation is challenged, an appraisal of the property by a qualified and certified appraiser(s) shall be offered by the potential subsidizer. If the parties cannot agree on a valuation through negotiation, an average of the two appraisals shall be used as the basis of the interim formula. The rate of return to be applied to the value of the properties shall be estimated in accordance with the procedures described in § 1125.7.

#### § 1125.4 Revenue attributable to the rail properties.

The revenue attributable to the rail properties of a branch is the total of the revenues assigned to the branch in accordance with this section, plus any

subsidy payments that would cease upon discontinuance of service on the branch, for the subsidy year. The revenues assigned shall be derived from the following accounts:

(a) *Account 101—Freight.* The revenues assigned under this account shall be the actual revenues accruing to the railroad, derived from waybills and other source documents for all traffic that:

(1) Originates and terminates on the branch;

(2) Originates or terminates on the branch and is handled off the branch on the system but not on another carrier; and,

(3) Originates or terminates on the branch and is handled on another carrier.

The revenues of all bridge or overhead traffic shall be attributed to the branch on the basis of the ratio of miles moved on the branch to miles moved on the system.

(b) *Account 102—Passenger; Account 104—Sleeping car; and Account 105—Parlor and chair car.* The revenues assigned under these accounts shall be the amounts in the railroad's accounts apportioned to the branch on the basis of the ratio of passenger car-miles on the branch to passenger car-miles on the system of the railroad.

(c) *Account 103—Baggage; Account 106—Mail; Account 107—Express; Account 108—Other passenger train; Account 109—Milk; and Account 131—Dining and buffet.* The revenues assigned under these accounts shall be the amounts in the railroad's accounts apportioned to the branch on the basis of the ratio of passenger car-miles on the branch to passenger car-miles on the system of the railroad.

(d) *Account 110—Switching; Account 113—Water transfers; Account 132—Hotel and restaurant; Account 133—Station, train, and boat privileges; Account 135—Storage—Freight; Account 137—Demurrage; Account 138—Communication; Account 139—Grain elevator; Account 141—Power; Account 142—Rents of buildings and other property; Account 143—Miscellaneous; Account 151—Joint facility, Cr.; and Account 152—Joint facility, Dr.* The revenues assigned under these accounts shall be the actual revenues accruing to the rail road that are directly attributable to the branch.

§ 1125.5 Avoidable costs of providing service.

The avoidable costs of providing service on a branch are the total of the costs assigned or apportioned to the

branch in accordance with this section. All on-branch costs, whether direct or allocated, shall be computed separately for freight and passenger services. Costs apportioned under paragraphs (a) through (k) of this section shall be derived from the latest Form R-1 of the railroad filed with the Commission prior to the conclusion of the subsidy year. Labor costs must be identified separately for all accounts when costs are assigned on a direct basis.

(a) *Maintenance of way and structures—(1) Account 202—Roadway maintenance; Account 212—Ties; Account 214—Rails; Account 216—Other track material; Account 218—Ballast; and Account 220—Track laying and surfacing.* The costs assigned under these accounts shall be the actual branch costs assigned on a direct basis.

(2) *Account 206—Tunnels and subways; Account 208—Bridges, trestles and culverts; Account 210—Elevated structures; Account 221—Fences, snowsheds, and signs; Account 227—Station and office buildings; Account 229—Roadway buildings; Account 231—Water stations; Account 233—Fuel stations; Account 235—Shops and engine houses; Account 237—Grain elevators; Account 239—Storage warehouses; Account 241—Wharves and docks; Account 243—Coal and ore wharves; Account 244—TOFC and COFC terminals; Account 247—Communications systems; Account 249—Signals and interlockers; Account 253—Power plants; Account 257—Power—transmission systems; and Account 265—Miscellaneous structures.* The costs assigned under these accounts shall be the actual branch costs assigned on a direct basis. A cost may not be assigned under one of these accounts unless the facility to which it pertains is in use for rail transportation purposes and its only useful purpose is to serve the branch.

(3) *Account 272—Removing snow, ice, and sand; Account 273—Public improvements—Maintenance; Account 278—Maintaining joint tracks, yards, and other facilities—Dr.; Account 279—Maintaining joint tracks, yards, and other facilities—Cr.; Account 281—Right-of-way expenses; and Account 282—Other expenses.* The costs assigned under these accounts shall be the actual branch costs assigned on a direct basis.

(b) *Maintenance of Equipment—(1) Account 311—Locomotives—Repairs.* This account shall be separated between yard and other (road) with a further separation between diesel and other elec-

tric). The costs assigned under this account for yard locomotives shall be apportioned to the branch separately for diesel and electric locomotives on the basis of the ratio of branch diesel and electric yard locomotive unit-hours to the total system diesel and electric yard locomotive unit-hours. The costs assigned under this account for other locomotives (road) shall be apportioned to the branch separately for diesel and electric locomotives on the basis of the ratio of branch diesel and electric locomotive gross ton-miles in road service to the total system diesel and electric locomotive gross ton-miles in road service.

(2) *Account 317—Passenger—train cars—Repairs.* The costs assigned under this account shall be the actual branch costs assigned on a direct basis. If the costs cannot be assigned on a direct basis, the amount in the railroad's account shall be apportioned to the branch on the basis of the ratio of branch passenger car-miles to the railroad's total passenger car-miles.

(3) *Account 318—Highway revenue equipment—Repairs.* The costs assigned under this account shall be the actual branch costs assigned on a direct basis.

(4) *Account 323—Floating equipment—Repairs; Account 326—Work equipment—Repairs; Account 328—Miscellaneous equipment—Repairs; Account 329—Dismantling retired equipment; and Account 330—Retirements—Equipment.* The costs assigned under these accounts shall be the actual costs that are directly attributable to the branch.

(5) *Account 331—Equipment—Depreciation—(52) Locomotives—Yard.* This account shall be included if the branch is serviced by a yard locomotive. The cost shall be assigned to the branch on the basis of the ratio of locomotive unit-hours on the branch to total locomotive unit-hours on the system.

(52) *Locomotives—Other.* When a branch is served by a local/way or through train crew the expense shall be assigned to the branch on the basis of the ratio of locomotive unit hours on the branch to the total locomotive unit-hours on the system.

(53) *Freight-train cars.* On-branch car costs shall be calculated on the basis of system average day and mileage ratios. This is an element in the cost per car-day and per car-mile calculation.

(54) *Passenger train cars.* In those instances where passenger service is offered on the branch, this expense shall be assigned to the branch on the basis of the ratio of passenger car miles on the

branch to the passenger car-miles on the total system.

(55) *Highway revenue equipment.* Only equipment which is specialized in its capacity and/or would not be used elsewhere in revenue service may be included. The inclusion of the expense shall be on an actual basis only.

(56) *Floating equipment.* Expenses relating to equipment under this category for which there would be no further need may be included on an actual basis only.

(6) *Account 336—Joint maintenance of equipment expenses—Dr.; Account 337—Joint maintenance of equipment expenses—Cr.; and Account 339—Other expenses.* The costs assigned under these accounts shall be the actual costs that are directly attributable to the branch.

(c) *Transportation—Rail Line.—(1) Account 372—Dispatching trains; Account 373—Station employees; Account 374—Weighing, inspection, and demurrage bureaus; Account 375—Coal and ore wharves; Account 377—Yardmasters and yard clerks; Account 379—Yard switch and signal tenders; and Account 407—Communication system operation.* The costs assigned under these accounts shall be the actual branch costs assigned on a direct basis and will be assignable only if it can be demonstrated that such costs would be avoided as a result of the service being discontinued.

(2) *Account 376—Station supplies and expenses; and Account 389—Yard supplies and expenses.* The costs assigned under these accounts shall be the actual branch costs assigned on a direct basis.

(3) *Account 378—Yard conductors and brakemen; and Account 380—Yard enginemen.* These costs shall be assigned only on a direct basis.

(4) *Account 382—Yard switching fuel.* The costs assigned to this account shall be the amount in the railroad's account apportioned to the branch on the basis of the ratio of yard diesel locomotive unit-hours on the branch to the railroad's total yard diesel locomotive unit hours.

(5) *Account 383—Yard switching power produced; and Account 384—Yard switching power purchased.* The costs assigned to these accounts shall be the amount in the railroad's accounts apportioned to the branch on the basis of the ratio of electric yard locomotive unit-hours on the branch to the railroad's total electric yard locomotive unit-hours.

(6) *Account 388—Servicing yard locomotives.* The costs assigned to this account shall be the amount in the railroad's account apportioned to the branch on the basis of the ratio of branch yard



locomotive unit hours to the railroad's total yard locomotive unit hours.

(7) *Account 392—Train enginemen; and Account 401—Trainmen.* These costs shall be the actual branch costs assigned on a direct basis.

(8) *Account 394—Train fuel.* If the branch is served by a local/way or through train crew, the costs assigned under this account shall be the amount in the railroad's account apportioned to the branch on the basis of the ratio of branch diesel locomotive unit-hours (road) to the railroad's total diesel locomotive unit-hours (road).

(9) *Account 395—Train powered produced; Account 396—Train power purchased.* The costs assigned to these accounts shall be the amounts in the railroad's accounts apportioned to the branch on the basis of the ratio of branch electric road locomotive unit hours to the railroad's total system electric road locomotive unit hours.

(10) *Account 400—Servicing train locomotives.* If the branch is served by a local/way or through train crew, the costs assigned under this account shall be the amount in the railroad's account apportioned to the branch on the basis of the ratio of branch locomotive unit-miles (road) to the railroad's total locomotive unit miles (road).

(11) *Account 402—Train supplies and expenses.* If the branch is served by a local/way or through train crew, the costs assigned under this account shall be the amount in the railroad's account apportioned to the branch on the basis of the ratio of branch train hours to the railroad's total train-hours. However, heater and refrigerator charges and credits may not be included in Account 402 unless they are applicable to the branch.

(12) *Account 404—Signal and interlocker operation; and Account 405—Crossing protection.* The costs assigned under these accounts shall be the actual branch costs assigned on a direct basis.

(13) *Account 406—Drawbridge operation; and Account 408—Operating floating equipment.* The costs assigned under these accounts shall be the actual branch costs assigned on a direct basis, but only if those costs are incurred for the exclusive use of the branch.

(14) *Account 411—Other expenses; Account 415—Clearing wrecks; Account 416—Damage to property; Account 417—Damage to livestock on the right-of-way; Account 418—Loss and damage—Freight; Account 421—TOFC/COFC terminals; Account 422—Other highway transportation expenses; Account 390—Operating joint yards and terminals—*

*Dr.; Account 391—Operating joint yards and terminals—Cr.; Account 412—Operating joint tracks and facilities—Dr.; and Account 413—Operating joint tracks and facilities—Cr.* The costs assigned under these accounts shall be the actual branch costs assigned on a direct basis.

(d) *Miscellaneous Operations.—Account 441—Dining and buffet service; Account 442—Hotels and restaurants; Account 443—Grain elevators; Account 445—Producing power sold; Account 446—Other miscellaneous operations; Account 447—Operating joint miscellaneous facilities—Dr.; and Account 448—Operating joint miscellaneous facilities—Cr.* The costs assigned under these accounts shall be the actual branch costs assigned on a direct basis.

(e) *Fringe benefits.* (1) Fringe benefits shall be assigned on a basis of a percentage of direct wages. The percentage shall be developed by using data from the railroad's latest Form R-1. The total of all health and welfare accounts (Accounts 277, 335, 359, 409, 449, and 456) taken from Sch. 320, col. (b) shall be added to the total of payroll taxes, old-age retirement and unemployment insurance, taken from Sch. 350, and divided by the total employee compensation taken from Sch. 320, col. (b). The resulting percentage shall be applied to the direct labor costs relating to maintenance of way and structures, transportation, and miscellaneous expenses.

(2) Since direct labor costs are not available for maintenance of equipment, the railroad shall be required to furnish a ratio of labor costs to total maintenance of equipment expenses. The ratio shall be applied to the maintenance of equipment costs assigned to the branch to develop an estimate of the related labor costs. The percentage developed in the preceding paragraph shall then be applied to the estimated labor costs to develop the fringe benefit costs for maintenance of equipment.

(f) *Revenue taxes.* The amount of revenue taxes shall be computed based on the amounts directly paid in those States that subject the railroad to a revenue tax.

(g) *Property taxes.* The amount of property taxes shall be the amount levied against the property on the branch, in those States where a true ad valorem tax is levied, based on the value of certain kinds of railroad property such as track, land buildings, and other facilities. In States where property taxes are levied on the basis of a formula of a State-wide valuation of property, the railroad shall support any claim of savings for property taxes in the event of abandonment of

the branch. If the railroad would realize State-wide savings on the basis of a proposed discontinuance of service on more than one branch operated in that State, the amount assigned to that branch shall be apportioned on the basis of the ratio of the miles of track on that branch to the railroad's miles of track proposed for discontinuance in that State.

(h) *Rent income.—(1) Account 503—Hire of freight cars and highway revenue equipment—Credit balance.* The amount assigned under this account shall be based on a special analysis of the highway revenue equipment used exclusively on the branch.

(2) *Account 504—Rent from locomotives; Account 505—Rent from passenger-train cars; Account 506—Rent from floating equipment; and Account 507—Rent from work equipment.* The amounts assigned under these accounts shall be based on the actual receipts for the kind of equipment rented, but may not be included unless the kind of equipment rented is normally used exclusively for branch traffic.

(3) *Account 508—Joint facility rent income.* The amounts assigned under this account shall be the actual branch receipts assigned on a direct basis.

(i) *Rents Costs.—(1) Account 536—Hire of freight cars and highway revenue freight equipment—Debit balance.* The amount assigned under this account shall be based on a special analysis of the highway revenue equipment used exclusively on the branch.

(2) *Account 537—Rent for locomotives; Account 538—Rent for passenger-train cars; and Account 539—Rent for floating equipment.* If the equipment is used exclusively for branch traffic, the costs assigned under these accounts shall be the actual branch costs assigned on a direct basis. If analysis shows common rents, the common rents cost shall be apportioned to the branch on the basis of the ratio of applicable locomotive, passenger-train car, or floating equipment days or miles, as used for billing purposes, on the branch to the total of those days or miles on other lines of the railroad.

(3) *Account 540—Rent for work equipment.* The costs assigned under this account shall be the actual branch costs assigned on a direct basis.

(4) *Account 541—Joint facility rents.* The costs assigned under this account shall be the actual branch costs assigned on a direct basis, plus, for common expenses, an apportionment of common expenses to the branch on the basis of

the ratio of the branch total in Accounts 278, 336, 390, and 412 to the railroad's total in those accounts.

(j) *Freight train car costs.* The on-branch costs for time-mileage freight-train cars shall be calculated on the basis of the railroad's average costs per day and per mile. These costs shall include Account 314—Freight train cars—Repairs; Account 331 (53) Equipment—Depreciation of freight train cars; freight car portion of Account 503—Hire of freight cars and highway revenue equipment—Credit balance; freight car portion of Account 536—Hire of freight cars and highway revenue equipment—Debit balance; and the return on investment in freight-train cars. The system totals for repairs and depreciation shall be divided into time related costs and mileage related costs on the basis of the standard Rail Form A apportionment factors (i.e., 50 percent time and 50 percent mileage for repairs, and 60 percent time and 40 percent mileage for depreciation). Return on investment shall be treated as a 100 percent time related cost. The system total receipts and payments for the hire of time-mileage cars and the basic data used in the development of the car-day and car-mile factors shall be taken from the railroad's latest Form R-1. The specific steps to complete the calculations are as follows:

(1) The total system car-days shall be calculated as follows: freight car ownership at the beginning and ending of the year (R-1, Sch. 417, line 69, cols. n and w); multiplying the average by the standard active number of car-days per car (346) as developed in ICC Docket number 31358; subtracting car-days on foreign lines (R-1, Sch. 376, lines 15 and 16, col. (c)); and adding the foreign car days on home line (R-1, Sch. 376, lines 15 and 16, col. (d)).

(2) The total railroad car miles shall be calculated by adding the loaded car miles (R-1, Sch. 531, line 12, col. (d)) to the empty car miles (R-1, Sch. 531, line 14, col. (d)).

(3) The cost per car-day shall be calculated by adding 50 percent of the railroad's total freight-train car repair cost (R-1, Sch. 320, line 74, col. (b)); 60 percent of the railroad's total freight-train car depreciation costs (R-1, Sch. 330, line 3, col. (b)); 100 percent of the railroad's return on investment on freight-train cars (Rail Form A, Form 2, line 20, col. (6)); the time portion of the railroad's payments for the hire of time-mileage freight-train cars (R-1, Sch. 376, line 14, col. (d)); subtracting the time portion of the railroad's receipts for hire of time-mileage freight train cars (R-1, Sch. 376,



line 14, col. (c)); and dividing the result by the total system car-days developed in paragraph (j) (1) of this section.

(4) The cost per car-mile shall be calculated by adding 50 percent of the railroad's total freight-train car repair cost (R-1, Sch. 320, line 74, col. (b)); 40 percent of the railroad's total freight-train car depreciation costs (R-1, Sch. 330, line 3, col. (b)); the mileage portion of the railroad's payments for the hire of time-mileage freight-train cars (R-1, Sch. 376, line 8, col. (d)); subtracting the mileage portion of the railroad's receipts for the hire of time-mileage freight-train cars (R-1, Sch. 376, line 8, col. (c)); and dividing the result by the total system car-miles developed in paragraph (j) (2) of this section.

(5) The costs per car-day and per car-mile developed in paragraph (j) (4) of this section shall be applied to the total car-days and total car-miles accumulated on the branch for all traffic originated and/or terminated on the branch and all bridge traffic handled by the branch during the subsidy period which are attributable to time-mileage freight-train cars. The car-day and car-mile factors shall be furnished by the railroads. The on-branch costs for freight-train cars rented on a straight mileage basis shall be the system average cost per car-mile applied to the total car-miles accumulated on the branch, loaded and empty. The average cost per car-mile is developed from the railroad's latest Form R-1, Sch. 376, or as follows: col. (d) plus col. (f) divided by col. (b), (using line 1 for tank cars, line 2 for refrigerator cars, line 5 for TOFC/COFC cars and line 3 for all other cars).

(k) *Off-branch costs.* (1) Certain terminal costs, line-haul car costs, and interchange costs shall be considered as the off-branch avoidable costs of providing service over the remainder of the railroad's system. These costs shall be computed by applying variable unit costs to the service units attributed to the branch traffic during the subsidy period.

(2) The following through train single line variable unit costs shall be developed by the railroad by applying data contained in its latest Form R-1 filed with the Commission to Rail Form A: cost per carload by car type, modified cost per carload by car type (substitute an inter-train switching cost, separated between mileage and other than mileage cars, for a road train to industry switching cost; and substitute a modified car ownership cost developed in accordance with section 1125.5(j) above using an allowance of two days in the terminal to cover the loaded and empty car movement for the

standard car ownership costs; cost per car-mile by car type; cost per ton-mile; and cost per car interchanged, separated between mileage cars and other than mileage cars.

(3) Terminal costs shall be calculated by multiplying the modified costs per carload, by car type, by the total number of carloads originated or terminated on the branch during the subsidy year. To this amount add the regular costs per carload, by car type, times the number of carloads which originate or terminate on the branch that are local to the railroad serving the branch.

(4) The line haul costs shall be calculated by applying the costs per car-mile by car type to the loaded car-miles on the system by car type originated or terminated on the branch during the subsidy year and applying the ton-mile unit cost to the total ton-miles on the system of revenue freight in road service originated or terminated on the branch during the subsidy year and totaling the results.

(5) The interchange costs shall be calculated by multiplying the cost per car interchanged by the number of carloads of traffic interchanged that originated or terminated on the branch.

#### § 1125.6 Valuation of rail properties.

The value of the rail properties on a branch shall be determined in accordance with the following:

(a) Only the following properties on a branch may be considered:

(1) Those that are used and useful to provide the rail services requested by the person offering a subsidy.

(2) In the absence of a request for specific services by that person, those properties that are used and useful to provide the rail service performed on the branch at the time the final system plan becomes effective, or if no service was being performed at that time, the services that were last performed on the branch.

(b) The value of the properties shall be their net liquidation value for their highest and best use, consistent with applicable zoning and land use regulations, determined by computing their current market value for other than rail transportation purposes, less all costs of dismantling and disposition of improvement necessary to make the remaining property available for its highest and best use.

(c) If the railroad and person offering a subsidy cannot, within a period of time that either of them considers reasonable after the beginning of negotia-

tions for the payment of the subsidy, agree on the properties that are used and useful or the net liquidation value, or both, the one that considers that a reasonable period of time has elapsed may notify the other of its intention to have the matter arbitrated. Each of the parties shall then appoint a representative and the representatives shall select an arbitrator or arbitrators mutually acceptable to them. The decision of the arbitrator or arbitrators shall be final.

(d) If either party fails to appoint a representative within five days after receiving notice from the other party of its representative, or if the appointed representatives fail, within five days after the last one of them is appointed, to agree upon a mutually acceptable arbitrator or arbitrators, either party may submit the matter for arbitration to the American Arbitration Association pursuant to its commercial arbitration rules, and the decision of its arbitrator or arbitrators shall be final.

(e) In considering the value of properties under this section, the arbitrator or arbitrators shall consider, among other factors, any bona fide offer for the properties, or a part thereof, recent sales of adjoining or similar properties, and any available appraisals, by a reputable appraiser, of the properties, or a part thereof.

(f) If the person offering a subsidy is a public body, each meeting of an arbitrator or arbitrators with the parties for the purposes of receiving information or evidence or to hear arguments or views shall be open to the public. Any interested member of the public may file written views, argument, or information with the arbitrator or arbitrators at any time within 3 days after the closing of the sessions that are open to the public.

#### § 1125.7 Reasonable return on the value of the properties.

The reasonable return on the value of rail properties, as determined under § 1125.6, shall be the interest rate that is equal to the publicly quoted yield to maturity or earliest call date on the first business day of the month in which the subsidy agreement is entered into, for United States Treasury bonds or notes maturing or having an earliest call date approximately coterminous with the end of the subsidy period. United States Treasury bonds redeemable at par before call or maturity for the sole purpose of applying the proceeds to payment of Federal estate taxes, and Treasury notes Series EA or EO shall be excluded from consideration for this purpose.

#### § 1125.8 Submission of information by railroad giving notice of intent to discontinue service on a branch.

(a) A railroad giving notice of intent to discontinue service on a branch shall give to the Director of the Office, and to the governor and railroad regulatory commission of each State within which the branch is located and to any other person upon request an "Estimate of Subsidy Payment" including information prescribed in Appendix I to this Part.

(b) Beginning with the week in which it gives notice of intent to discontinue service on a branch, pursuant to section 304(a)(2)(B) of the Act, the railroad shall publish a copy of that notice of intent in a newspaper or newspapers of general circulation in the areas encompassing the branch at least once a week for three consecutive weeks.

(c) Each railroad providing the information required by paragraph (a) of this section, and publishing a notice as required by paragraph (b) of this section, shall include therein a statement to the effect that copies of the materials and information upon which the railroad's calculations for the purposes of § 1125.3 have been made are located at an office of the railroad within the State or States concerned and may be examined by any interested person during regular working hours. However, documents upon which the calculations are made which disclose information concerning the nature, kind, quantity, destination, consignee, or routing of traffic shall, if the railroad so requests, be shown only to a representative of the person offering a subsidy and only if that representative agrees to keep that information confidential.

(d) A notice of intent to discontinue (B) of the Act, is not considered to be completed or given until the railroad has taken the actions required by paragraphs (a) through (c) of this section.

(e) Each railroad must establish a system of collecting the cost and other relevant data required herein at the branch level.

(f) Each railroad must file a "Financial Status Report" including the information prescribed in Appendix II to this Part within 30 days after the end of each quarter of the subsidy year. Significant deviations from the original estimates must be explained. Unless the parties agree otherwise, the third quarter report will be the basis for negotiating the subsequent year subsidy agreement. The year-end report will be the basis of the subsidy payment adjustment.

(g) A railroad entering into a subsidy agreement shall make available, in the same manner and subject to the same conditions described in paragraph (c) of this section, to any interested person copies of the materials and information upon which calculations for the purposes of § 1125.4 through 1125.7 have been or are to be made.

#### APPENDIX I—INFORMATION TO BE FURNISHED

The following information is required to be furnished under § 1125.8(a). All data shall be developed in accordance with the methodology set forth in § 1125.3.

##### REVENUES ESTIMATED FOR

1. Freight Originated And/Or Terminated On Branch.
2. Bridge Traffic.
3. Demurrage.
4. Passenger.
5. All Other.
6. Total Estimated Revenues (lines 1 through 5).

##### AVOIDABLE COST ESTIMATES FOR

7. Off-Branch Costs (Ratio times line 1).
8. On-Branch Costs (lines 8a through 8f).
- a. Maintenance of Way and Structures.
- b. Rehabilitation.
- c. Maintenance of Equipment.
- d. Transportation.
- e. Taxes.
- f. Miscellaneous.
9. Total Avoidable Cost Estimate (line 7 plus line 8).

##### RETURN ON VALUE ESTIMATE

10. Valuation of Property.
11. Rate of Return.
12. Total Return on Value (line 10 times line 11).

##### ESTIMATED SUBSIDY PAYMENT

13. Estimated Subsidy Payment (line 6 minus lines 9 and 12).

#### APPENDIX II—INFORMATION TO BE FURNISHED

The following information is required to be furnished under § 1125.8(f). All data shall be developed in accordance with the methodology set forth in § 1125.4-7. The actual data for the year to date and a projection to the end of the subsidy year shall be shown for each item, except that off-branch costs shall be estimated during the subsidy year by applying the ratio developed in the interim formula to the actual revenues shown in item 1.

#### RULES AND REGULATIONS

##### REVENUES FOR

1. Freight Originated And/Or Terminated on Branch.
2. Bridge Traffic.
3. Demurrage.
4. Passenger.
5. All Other.
6. Total Revenues (line 1 through 5).

##### AVOIDABLE COSTS FOR

7. Off-Branch Costs (Ratio times Line 1).
8. On-Branch costs (lines 8a through 8f).
- a. Maintenance of Way and Structures.
- b. Rehabilitation.
- c. Maintenance of Equipment.
- d. Transportation.
- e. Taxes.
- f. Miscellaneous.
9. Total Avoidable Cost (line 7 plus line 8).

##### RETURN ON VALUE

10. Valuation of Property.
11. Rate of Return.
12. Total Return on Value (Line 10 times Line 11).

##### SUBSIDY PAYMENT

13. Subsidy Payment (line 6 minus lines 9 and 12).

[FR Doc. 75-170 Filed 1-7-75; 8:45 am]

#### ERRATA SHEET

Pg 1624, col. 1, para. 3, (beginning "The standards defined. . .") last line: should read "miles on the branch to passenger miles on the system."

Pg 1625, col. 2, line 5:  
"opportunity" should read "apportionment"

Pg 1625, col. 2, line 7:  
Delete "use of apportionment formulas for cer-"  
Insert "available. The tests revealed that in cer-"

Pg. 1627, col. 3, para. 2, line 13:  
"abandment" should read abandonment"

Pg 1631, col. 1, right before § 1125.1:  
"Pub. L. 92-236" should read "Pub. L. 93-236"

Pg. 1632, col. 1, para. (4), 11 lines from bottom:  
"accounts 372 and 401" should read "accounts 392 and 401"

Pg 1632, col. 2, para. (b), line 3:  
"Palor" should "Parlor"

Pg. 1632, col. 2, para. (b) lines 7 & 8:  
"passenger car-miles" should read "passenger-miles"

Pg. 1632, col. 2, para. (c), line 9:  
Delete "the basis of"

Pg 1633, col. 2, para. (9), line 1:  
"Train powered" should read "Train power"

Pg 1634, col. 1, para. (g), line 6:  
"porperty" should read "property"

Pg 1634, col. 1, para. (i), line 3:  
Delete "fright"

Pg 1634, col. 2, para. (j) (1), line 2:  
Delete "calculations are as follows:"  
Insert "calculated by averaging the railroad's"  
(40 Fed. Reg. 3216)

Pg. 1634, col. 3, top 2 lines:

Should read "(d) A notice of intent to discontinue service, pursuant to section 304(a)(2)"

Pg. 1636, para. 2, line 8a:

Indent line a 3 spaces

## APPENDIX D

# INTERSTATE COMMERCE COMMISSION



## RAIL SERVICE CONTINUATION SUBSIDIES

Standards For Determination

(March 28, 1975)  
(40 Fed. Reg. 14186)



## Title 49—Transportation

## CHAPTER X—INTERSTATE COMMERCE COMMISSION

## SUBCHAPTER B—PRACTICE AND PROCEDURE

[Ex Parte No. 293 (Sub-No. 2)]

## PART 1125—STANDARDS FOR DETERMINING RAIL SERVICE CONTINUATION SUBSIDIES

## Miscellaneous Amendments

On February 25, 1974, (39 FR 7182), the Director of the Rail Services Planning Office (Office) of the Interstate Commerce Commission (Commission) issued a notice of proposed rulemaking and order, pursuant to section 205(d)(3) of the Regional Rail Reorganization Act of 1973 (Act) which provides that the Rail Services Planning Office shall: " \* \* \* within 180 days after the date of enactment of this Act, determine and publish standards for determining the "revenue attributable to the rail properties," the "avoidable costs of providing service" and "a reasonable return on the value," as those phrases are used in section 304 of this Act, after a proceeding in accordance with the provisions of section 563 of Title 5, United States Code \* \* \*".

After an extended period for public comment, the Office issued standards on July 1, 1974, (39 FR 24294). On July 30, 1974, the Office issued a notice announcing that petitions seeking amendment of the standards would be accepted if filed on or before August 19, 1974, (39 FR 28196).

In requesting amendment of the standards, several parties urged that the standards be tested on actual branch lines and that the time for filing be extended. On September 10, 1974, the Office issued a notice stating that the standards would be tested and that the time for filing pleadings was being extended to October 30, 1974, (39 FR 33544).

Following an in-depth analysis of the petitions and of the knowledge gained from the testing of the standards, the Office published revised standards for determining rail service continuation subsidies on January 8, 1975, (40 FR 1624). Since the revised standards reflected significant changes from the original version, the Office invited additional comments to be filed by February 18, 1975.

## POSITIONS OF THE PARTIES AND DISCUSSION

Only 17 comments were filed in response to the Office's invitation and some of those did not suggest further modifications of the standards. There now appears to be a general consensus that the

conceptual approach taken is correct and that, with minor amendments, the standards are fair, equitable, and operable.

*General.* Many of the comments seem to stem from a lack of understanding of the relationship between the subsidy standards and Federal rail service continuation assistance.

Federal financial assistance is provided for under section 402 of the Act. The responsibility for administering the program is assigned to the Secretary of Transportation who has delegated his responsibilities to the Federal Railroad Administrator. The procedures and requirements regarding applications for and disbursement of Federal rail service continuation assistance were published on January 28, 1975, (49 CFR Part 255, 40 FR 4232). The rules provide, inter alia, that, if certain prescribed planning functions are followed, Federal matching funds will be made available to States on the basis of a 70/30 ratio. Under the FRA rules Federal matching funds will not be available if a State fails to perform its planning functions; (e.g., the development of a State rail transportation plan).

Under section 304 of the Act, rail service on rail properties of a railroad in the region which transfers to ConRail or to profitable railroads operated in the region all or substantially all of its rail properties designated for such conveyance in the Final System Plan may discontinue service and/or abandon the properties not designated for inclusion unless: (1) a shipper, a State, the United States, the local or regional transportation authority, or any responsible person offers a rail service continuation subsidy based upon the standards determined by this Office; (2) a subsidy is offered which is payable pursuant to an existing subsidy agreement; or (3) there is made an offer to purchase such rail properties in order to operate rail service over such properties. There is no requirement that Federal funds be involved in any of the offers. As a matter of fact, some states have constitutional limitations which will prevent them from participating in the Federal subsidy program, and a few states may fail to comply with the FRA rules. In those instances, the subsidy payment may have to be funded entirely through non-Federal sources. There is also a strong possibility that, with some subsidizers, the advantages of negotiating a subsidy agreement free of Federal and State influences would override the advantages of the matching funds. This

would be especially true when the subsidy payment is insignificant in relationship to the size of the branch or the subsidizer's ability to pay. Consequently, these standards may be applied in many situations not involving the expenditure of Federal matching funds.

This lack of understanding of the two programs has led to some confusion about the relative responsibilities of the Office and FRA in promulgating the standards for the respective programs. While section 402(f) limits the length of the term of the subsidy agreement involving Federal funds to two years, there is no such limitation with respect to a subsidy agreement which does not involve Federal funds.

It has also been suggested that Congress amended the Act (Pub. L. 93-488) to limit applications of Federal funds to rail freight services, thereby excluding passenger services. It is not the role of this Office, at least in this forum, to determine whether the intent of the amendment was to exclude passenger services from Federal assistance under section 402. It is clear, however, that the amendment only pertains to section 402 and does not amend section 304. Consequently, even assuming arguendo that passenger service is not eligible for section 402 funds, the amendment has no impact on section 304 subsidy offers, as they do not necessarily involve Federal funds.

The practical problem of implementing the subsidy program after the Final System Plan is approved by the Congress gives rise to another line of comments. It is assumed, even though the United States Railway Association did not affirmatively so state in the Preliminary System Plan issued February 26, 1975, that ConRail will be the operating railroad for most of the lines which are not recommended for inclusion in the new system but for which a subsidy is offered. If such is the case, the negotiations of the subsidy agreement will involve three parties: the subsidizer; ConRail, and the trustees of the railroad owning the property. Section 304(c) of the Act provides that the operator of the rail service will receive the difference between the revenues attributable to properties and the avoidable cost for providing such service and the trustee shall receive a reasonable rate of return on the value of rail properties on which rail service is operated. Consequently, the subsidizer will be negotiating operational issues with ConRail and valuation issues with the trustees. While the standards do not specifically identify

this practicality they are flexible enough without modification to accommodate it. This situation was anticipated in the development of the definition of the word "railroad" in the standards. The standards provide that the term may mean "either the owner of the rail properties over which subsidized service is or may be performed, or the operator of that service or both."

The United States Department of Transportation (DOT), the Association of American Railroads (AAR), the Central Railroad Company of New Jersey (CNJ), and the Penn Central Transportation Company (Penn Central) continue to take issue with the Office's authority to issue comprehensive standards that will result in a formula by which a subsidy payment may be readily computed. The parties offer no new information or discussion of any issues which the Office did not consider when the present standards were adapted. Accordingly, the Office sees no reason to reconsider any issues relating to the Office's authority.

The CNJ indicates concern that the so-called "actual costs" used in the subsidy standards are historical numbers that will have no real value when the Final System Plan is implemented. It fails to recognize the flexibility of the standards. If it turns out that ConRail operates the CNJ lines proposed for abandonment, estimates of ConRail revenues and costs could be used in the interim calculation, and an adjustment taking into account ConRail's actual experience would take place at the end of the subsidy year.

Several parties have suggested that the revised standards be tested on actual branch lines. The Office considered such tests but due to the inherent flexibility built into the present standards it is impossible to make actual calculations unless there are parties available to negotiate many of the important issues. The Office does recognize, however, that it is important for the potential subsidizers to be able to estimate the subsidy amount. By using the computer program the United States Railway Association utilized in making its light density line recommendations, the Office will attempt to make necessary modifications to develop an estimated subsidy payment. It is believed that, even though negotiations between the parties could significantly change the estimated payment, the calculations will provide a good estimate of the range of the subsidy payment required. It should also be noted as a practical matter that while the standards require rehabilitation of track to Class I standards for those lines presently op-

erating under waivers by the FRA, the unavailability of labor, equipment and materials will result in minimum rehabilitation of subsidized lines during the first few years of the program.

It was also suggested that the Office should assure that the operating railroad does not have to use its own funds as operating capital, or if it does, provide that the operator be reimbursed for the use of the funds. The Office agrees that a requirement of advanced quarterly payments of the estimated subsidy payment would not only establish the subsidizers good faith but would assist in establishing his credit rating as well. The Office also believes that there are advantages to withholding the last payment until the actual data relating to the subsidy period is available. Such an arrangement would assure that the majority of the working capital is provided by the subsidizer and would encourage the operator to quickly settle the account for the year. The Office also recognizes that the FRA regulations provide that payment of Federal funds will follow the provision of service. However, since the timing of the payments is a matter of administration of the subsidy agreement, and, therefore, outside the scope of the Office's responsibility the Office will not prescribe rules regarding such payments. The parties will be able to negotiate this issue, but, if deferred payments are involved, the operating railroad should be compensated for the use of the working capital. Accordingly, such interest will be considered as an avoidable cost. The interest rate, as computed in section 1125.7, will be applied to a monthly proration of the estimated subsidy payment.

The CNJ also asserts that some of the data requested by the standards is not now available by that railroad. No other railroad has indicated that the data requested in the standards is unobtainable. As a practical matter this should not be a problem since there will be sufficient data developed through the planning process to make the interim calculation, and the final payment will be based on branch line data collected during the subsidy period.

Several parties, including the Center for Rural Manpower and Public Affairs, AAR, DOT, Penn Central, Pennsylvania DOT, and the New England Regional Commission commented on the 15 percent ceiling to end-of-year adjustments resulting from an increase in the estimated subsidy payment. The arguments include constitutional issues, lack of authority on the part of the Office, incentive to overestimate, and the necessity

for distinguishing between recurring and non-recurring expenses. While the Office continues to see advantages in establishing a ceiling to the subsidy payment for a given year, the arguments to the contrary have some merit. The fact that the New England Regional Commission, representing six New England States, favors modifying the rule indicates that the necessity for a fixed ceiling is not as important as the Office originally believed it to be. Accordingly, the standards will be modified to require a carryover only if the operator fails to notify the subsidizer of the fact in one of the first three quarterly Financial Status Reports required under section 1125.8(f) or if the increase results from an expense preapproved by the subsidizer. This modification will assure that the subsidizer is kept informed of the financial status of the line and will provide timely information either to secure the additional funds or to minimize the losses. It will also provide a means to cover expenses that were not anticipated but which both parties agree are necessary to the continued operation of the line.

The petitions contain considerable comment regarding the handling of rehabilitation costs under the subsidy program. Most parties suggest that the cost of rehabilitation must be spread over a longer period. This issue was raised during the prior comment period, and no new information was presented which persuades the Office to change the present rule requiring recovery of rehabilitation costs during the term of the subsidy agreement.

It was suggested that a procedure be adopted to check the necessity of rehabilitation. Since this Office has no power to direct the FRA or any state regulatory agency to conduct inspections of branch lines, it is impossible to require such an independent inspection of the condition of the facilities. The present standards do, however, require the operator to furnish the subsidizer with an estimate of costs on a specific project basis. This should facilitate a negotiated agreement as to the level of effort required before any rehabilitation work is performed. The unavailability of supplies, equipment, and labor will result in a situation where there is little probability that major rehabilitation work on light density lines will be performed in the next few years. As a result, the problem in the near term will probably be to get the operator to agree to a certain level of rehabilitation as opposed to an over-rehabilitation situation.

The AAR and the Penn Central have also suggested that the cost of administering the subsidy program should be an avoidable cost. The Office agrees that the costs of administering the program are clearly avoidable; however, the problem of defining such costs could be as difficult as developing the operational costs. Since the administrative costs will undoubtedly relate to the volume of traffic on the branch, it appears that a payment related to revenues would be appropriate. Neither of the parties suggested a method for identifying such costs. If it were done on an actual basis, the costs of collecting such data would result in another administrative cost. In order to avoid such compounding of costs, the Office will establish one-half of one percent of the annual revenues as a flat rate to cover all costs of administering the subsidy program.

**Revenues.** Several issues, including attributing revenue-cost differences of rerouted bridge traffic to the branch, the apportionment basis for certain accounts, and limiting the scope of the revenue attributable to the branch operation, were raised again. Each of these issues was addressed in the Office's prior report and since no new rationale has been presented, the Office sees no reason to reconsider them. The Pennsylvania DOT suggested that revenue accounts 103, 106, 107, 108, and 109 relating to passenger service should be allocated or assigned on a different basis. The types of revenue included in these accounts make direct assignment of these revenues impractical; however, the Office does recognize the need for a more definitive standard. Accordingly, section 1125.4(c) will be modified to specify that amounts will be apportioned to the branch only if such revenue items are earned by trains operating on the branch line.

**Avoidable Costs.** The on-branch cost portion of the revised standards generated the most comments, many of which covered the same areas of concern raised previously. Only those areas where new or additional data was introduced to support a particular position are considered herein.

The \$1,000 per mile minimum allowance for maintenance of way raised several comments. Basically, the railroads contend that \$1,000 per mile is unrealistically low and the non-railroad petitioners contend that the figure is high. The Office recognized in its January 8, 1975, report that the \$1,000 per mile maintenance of way figure is unrealistically low over the long term and encouraged the parties to negotiate a higher rate. However, the Office also recognized

that, as a practical matter, the railroads have failed to direct maintenance resources toward light density lines and that such lines can and have been operated for significant periods of time with little or no maintenance. Accordingly the Office sees no reason to modify the standards in this regard.

Borden, Inc., suggested that accounts 278—*Maintaining joint tracks, yards, and other facilities—Dr.*, 279—*Maintaining joint tracks, yards and other facilities—Cr.*, 281—*Right-of-way expenses*, and 282—*Other expenses* be included only if they are required for the continued operation of the branch line or were requested by the subsidizing body. The present standards provide that costs assigned to these accounts be the actual branch costs assigned on a direct basis. The Office believes that the assignment basis presently used in the standards and the suggested change by the petitioner are similar and no further modification is necessary.

Borden, Inc., also recommended that accounts 329—*Dismantling retired equipment* and 330—*Retirement—Equipment* be further clarified. The petitioner asserts that the subsidizing body should not have to pay the cost of retiring equipment for a prior year when the subsidy period begins the following January. The petitioner was not explicit as to what should be clarified in regards to these two accounts. Since the standards presently include only costs that are directly attributable to the branch during the subsidy year, the Office sees no merit in the petitioner's contention.

This petitioner also recommended that account 331—*Equipment—Depreciation* should be deleted in its entirety from the standards citing two Commission decisions in abandonment cases where the Commission held that depreciation was not an allowable out-of-pocket expense. The petitioner, has attempted like many others, to compare the subsidy standards with abandonment cases. This is not a valid comparison. The subsidy standards are designed in accordance with the Act to define the cost of providing service and not the cost of abandoning service.

It was also suggested that equipment depreciation should be included only if the equipment is solely related to the branch. Since few light density lines will have equipment assigned on a full-time basis, the only rational way to determine the branch-related portion is a method of allocation based on a service unit factor that is a function of the use of the equipment being assigned to the branch.



Two petitioners contend that the interim formula's method of computation of through train costs results in an overstatement of the crew costs and that the same methodology used to develop local/way and yard crew costs should be used to have compatibility between the various types of crew costs. After reviewing this contention the Office finds there is merit to the contention and the standards will be amended accordingly to reflect the same methodology used to develop local/way and yard crew costs.

Several petitioners assert that the allocation of train supplies and expenses on the basis of train-hours overstates the amount assignable to the branch and that the more appropriate service unit factor is car-miles. Analysis of the types of expense items chargeable to account 402—*Train supplies and expenses* indicates that a majority of the items of expense are more related to a time factor than to a distance factor; and, therefore, the car-mile factor advocated by the petitioners is rejected.

Another petitioner has recommended that the explanation covering section 1125.5(c) (12) and (14) and 1125.5(d) be expanded to include "for the exclusive use of the branch." The standards state that costs assigned under these accounts shall be the actual branch costs assigned on a direct basis. The Office believes that assigning such costs on a direct basis will more nearly reflect the avoidable costs of providing service and that the limitation "of exclusive use of the branch" may be too restrictive in certain instances.

The inclusion of account 415—*Clearing wrecks*, according to one petitioner, should be included only if the cause of the derailment can be totally attributable to the branch. The Office sees no way that this burden can be shifted from the branch. Regardless of the cause of the derailment, the costs assigned to account 415 are clearly costs which would not be incurred if service on the branch was discontinued.

The AAR contends that the crew costs are understated because the costs are based on straight time hours. They state that overtime should be included because many of the branch lines operate on an overtime basis. It is true that some overtime may be incurred on a branch; however, it is not possible to assign it equitably to a particular branch since there is no control over where a crew works during its regular time. Furthermore, the difference is less significant than might at first appear since constructive allowances, vacation

and holiday pay are earned on straight time and not overtime.

The AAR and Penn Central questioned the exclusion of a number of overhead accounts contending that omission of these accounts distorts the actual cost. They pointed to the *Accountants' Handbook* which states that the assignment of all overhead costs will prevent an understatement of project costs. These contentions were raised previously by these petitioners and they have submitted no new data to cause the Office to revise the standards in this respect. It should be pointed out that the reference made to the *Accountants' Handbook* relates to a standardized manufacturing cost accounting system which is not related to railroad cost accounting.

According to AAR the revised standards will underestimate branch line operating costs because joint operations and facility costs involving the branch and main line have not been considered. The standards do recognize both the revenues and costs relating to these items contrary to petitioner's statement. The off-branch costs reflect the costs associated with joint operations and facilities to the extent these costs are incorporated in the variable costs developed by the application of Rail Form A.

The calculation of car costs by identifying car-miles and car-days by car type and applying it to the per diem rate by car type was advocated by the New England Regional Commission rather than the method based on system average car costs which is used in the standards. The use of the suggested calculation is rejected by the Office because it would be overly complex to apply and per diem rates contain an element of profit.

Penn Central contends that the calculation of freight train car costs has omitted certain rental expenses included in schedule 376 of the Annual Report, i.e., line 17, *Leased Rental-Railroad, Insurance and Other Companies*; line 18, *Other Bases* and; line 21, *Auto Racks*. After reviewing this contention, the Office finds that rental expenses relating to these items are properly includable in the calculation of car-mile and car-day costs and will be so reflected in the standards.

In reviewing the standards, it was noted that "col. (d)" in section 1125.5(j) (2), should read "col. (b)" and "col. (b)" in section 1125.5(j) (3) should read "col. (e)." These inadvertent errors are corrected in the revisions to the standards published herewith.

The comments regarding the off-branch costs related primarily to the appropriateness and uncertainty of using variable costs developed through the application of Rail Form A to the Carrier Annual Report (Form R-1) as the proper level for reimbursement. These issues were discussed in the January 8, 1975, report and the additional comments do not reveal any new considerations which require further comment or modification of the standards.

*Investment base and reasonable return on the value.* Comments from several of the parties were directed to the valuation of rail properties, the valuation arbitration procedures and the reasonable return on the value of the properties.

The National Industrial Traffic League (NITL) urges that the valuation be limited to the net carrier investment in the property involved. The absence of such a limitation, it is argued, could result in the carriers increasing the alleged investment base by designating the property for abandonment. It is possible that in some instances net liquidation value could exceed original cost less accrued depreciation; in other instances it may well be less. Under the circumstances most likely to occur under section 304 of the Act, the person receiving the return will not be a carrier, but the trustee of a debtor estate whose carrier responsibilities, at least as to the properties involved, will have been assumed by Con-Rail or some other operator under the subsidy agreement. It would be unfair in these circumstances to impose such a limitation.

The Pennsylvania DOT notes that the value of rail properties must be appraised on the basis of there being no rail service present and fears that the consideration of recent sales of adjoining or similar properties which had rail service may bias the appraisal. The point has merit and should be brought to the attention of the appraisers or arbitrators at the time of such appraisal or arbitration. The Office sees no need to include all such possibilities in the standards.

Penn Central, on the other hand, reiterates that the regulations should not attempt to define the value, and that in any case the definition should not exclude consideration of the value for railroad purposes. It contends that an abandonment under section 304 of the Act, in contrast to one under section 1(18) of the Interstate Commerce Act, is precipitated by the decision of the United States Railway Association that the particular line is not to be included in Con-Rail, rather than by a decision of railroad management. This appears to be

an erroneous analysis. Exclusion of any line from the system does not obligate the trustees to discontinue service under section 304(a) but rather merely permits them to do so unless an offer to purchase or sublease is made. Should the trustees consider that the best performance of their duties as fiduciaries is to continue rail operations over the line in question, they are not debarred by the Act from doing so.

The AAR recommends again that "fair market value" be substituted for net liquidation value, and that the standards incorporate instructions to the appraisers as to details to be considered in arriving at the value. For reasons stated in the discussion accompanying the January 8, 1975, standards publication, these recommendations have not been adopted.

The Penn Central urges that the arbitration award should be subject to review by the Reorganization Court, and that provision should be made for periodic reappraisal. Court review is available under the provisions of 9 U.S.C., 10-12, and reappraisal of the value can be obtained, if any party desires, at the time of each subsidy agreement renewal. It appears unnecessary to stipulate these matters in the subsidy standards.

The AAR urges that the arbitration be voluntary, not mandatory or binding. It is not mandatory if the parties can agree on a valuation. To provide for arbitration which is not binding would appear to serve no useful purpose and would be contrary to the very definition of the term.

The Center for Rural Manpower and Public Affairs and other parties recommend that the arbitrator be instructed, rather than deciding on the merits, to choose the value submitted by one of the parties which is nearest his own appraisal. Although this practice is understood to have been adopted in the sports field, it is not prevalent in commercial arbitration procedures; its legality and fairness in the circumstances contemplated here could be questioned; and it is by no means clear that the expense to the parties would be reduced.

As to the return on the value, the AAR again contends that it should be based on calculations the Office of Management and Budget (OMB) developed for distinctly different circumstances and purposes; that it should assume a hypothetical but unproven combined State and Federal income tax rate as high as 51 percent applicable to the trustees; and that flexibility in the rate of return is undesirable, since the "aggregate opportunity cost of capital to the investing



public changes very slowly, and certainly not on a year-to-year basis." These observations appear to be based on an imperfect reading of the Act, which directs the Office, not another agency, to determine and publish standards for a reasonable return on the value as that phrase is used in section 304 of the Act; on a misunderstanding of the circumstances under which such reasonable rate of return would be applicable; and on inattention to the course of publicly-quoted bond and stock yields during the past year.

The Penn Central with more cogency, again argues for some premium over the yield on marketable U.S. Government securities to take account of the risks and liquidity of each subsidy agreement. It suggests that the determination of such premium be left open for negotiation on a case-by-case basis, subject to final decision by the Reorganization Court. It refers to the credit difficulties currently involving certain "moral obligation" bonds.

The Office, in the explanatory material published January 8, 1975, described some of the difficulties it had experienced in endeavoring to evolve a basis for a premium sufficiently flexible to account for differences in credit status as between various subsidizing bodies.

Possible variations in the credit status of prospective subsidizers in relation to the fiduciary duties of the trustees do present difficulties, the scope of which cannot presently be foreseen. These have been mitigated by the provision that interest accrue on deferred installments of the estimated subsidy; this would bring into such payments an element of "interest on the interest." In any event, section 304 of the Act does not require the trustees to enter into contracts with irresponsible persons.

Negotiation between the parties as to all elements of the subsidy agreements is encouraged, but although the Office cannot preempt the jurisdiction of the courts it is not apparent that its duties under section 205(d)(3) of the Act could be discharged by leaving the standard for reasonable return on the value open to the suggested process.

For the reasons given above, and subject to these explanatory comments, §§ 1125.6 and 1125.7 of the standards will remain as published January 8, 1975. Contentions raised by the parties and not specifically addressed herein have nevertheless been considered and determined to be without merit.

#### PARTIES FILING PETITIONS

##### GOVERNMENT

Federal—Office of the Public Counsel, Rail Services Planning Office, United States Department of Transportation.

State—Commonwealth of Pennsylvania Department of Transportation, New York State Department of Transportation, Pennsylvania Public Utility Commission and the Pennsylvania State Legislative Board, United Transportation Union (jointly).

Regional—New England Regional Commission.

##### BUSINESS

Agrico Chemical Company, Archer Daniels Midland Company, CP Industries, Inc., Evans Products Company, FS Services, Inc., Illinois Grain Corporation, International Minerals & Chemical Corporation, Royster Company, and Swift Chemical Company (jointly), Borden Chemical Division, Borden, Inc., Mortgage Bondholder's Protective Committee of the Central Railroad Company of New Jersey, Georgia-Pacific Corporation.

##### ORGANIZATIONS

Center for Rural Manpower and Public Affairs, Citizens for Sound Planning, National Industrial Traffic League.

##### RAILROADS

Association of American Railroads, Central Railroad Company of New Jersey, Penn Central Transportation Company.

##### CONCERNED CITIZENS

Fayette B. Shaw, Ph. D.

##### ORDER

In consideration of the foregoing: *It is ordered*, That Part 1125 of Subchapter B of Chapter X of Title 49 of the Code of Federal Regulations, be amended by making the changes set forth below to the standards adopted on January 8, 1975.

*It is further ordered*, That this order shall become effective March 28, 1975.

[SEAL]

ROBERT L. OSWALD,<sup>1</sup>  
Secretary.

1. Delete the period (.) from the last sentence of § 1125.1(c) and add " . . . unless the railroad notifies the subsidizer that the estimate will be exceeded by more than 15 percent in one of the first three quarterly Financial Status Reports required by § 1125.8(f); or the increase results from an expense preapproved by the subsidizer."

2. Delete § 1125.3(c)(4) and insert in lieu thereof:

<sup>1</sup> Present: Alan M. Fitzwater, Acting Director, Rail Services Planning Office, to whom the matter under consideration in this docket has been assigned.

(4) Transportation costs shall be estimated, based upon system average costs. The number of trips per year shall be based upon the frequency of service performed at the time the notice is filed unless the parties agree to a different level. Labor costs for train crews shall be based on system average costs for each type of crew applied to the hours of service on the branch. The crew costs shall be classified into four major categories: Yard, local/way, through, and passenger. The straight time average cost per hour for each yard, local/way or through train crew member shall be calculated using the railroad's Employees, Service, and Compensation Report (Form B) for the base year. The calculation is made by adding together the straight time compensation, col. (9), and the constructive allowances, col. (11), and dividing this total by the straight time hours actually worked, col. (4). This process would be repeated for each yard, local/way and through train class of employee. After the hourly rate is determined for each member, the cost per crew hour shall be calculated based on the exact size and consist of the crew currently serving the branch. The crew cost per hour is multiplied by the estimated hours that will be incurred in serving the branch during the subsidy period. The estimated direct crew costs must be increased to cover fringe benefits using the procedure described in section 1125.5(e). The railroad shall also furnish estimates of costs for the remaining transportation accounts using the final standards as a guide to their includability and basis of calculation.

3. Delete the period (.) from the sentence found in § 1125.3(c)(6) and add: "plus an allowance for administrative costs based upon one-half of one percent of the revenues estimated in § 1125.3(a)."

4. Delete the sentence contained in § 1125.4(c) and insert in lieu thereof: "The revenues assigned under these accounts shall be apportioned to the branch on the basis of the ratio of passenger car-miles on the branch to passenger car-miles on the system of the railroad but only if such revenue is earned by trains operating on the branch line."

5. Delete "col. (d)" where it appears in § 1125.5(j)(2) and insert "col. (b)" in lieu thereof.

6. Delete § 1125.5(j)(3) and (4) and insert in lieu thereof:

(3) The cost per car-day shall be calculated by adding 50 percent of the railroad's total freight-train car repair cost (R-1, Sch. 320, line 74, col. (e)); 60 percent of the railroad's total freight-train car depreciation costs (R-1, Sch. 330, line 3, col. (e)); 100 percent of the railroad's return on investment on freight-train cars (Rail Form A, Form 2, line 20, col.

(6); the time portion of the railroad's payments for the hire of time-mileage freight-train cars (R-1, Sch. 376, line 14, col. (d) plus 50 percent of *Leased Rental—Railroad, Insurance and Other Companies* (R-1, Sch. 376, line 17, cols. (d) and (f)), *Other Basis* (R-1, Sch. 376, line 18, cols. (d) and (f)) and *Auto Racks* (R-1, Sch. 376, line 21, cols. (d) and (f)); subtracting the time portion of the railroad's receipts for hire of time-mileage freight-train cars (R-1, Sch. 376, line 14, col. (c)), and 50 percent of *Leased Rental—Railroad, Insurance and Other Companies* (R-1, Sch. 376, line 17, cols. (c) and (e)); *Other Basis* (R-1, Sch. 376, line 18, cols. (c) and (e)), and *Auto Racks* (R-1, Sch. 376, line 21, cols. (c) and (e)); and dividing the result by the total system car-days developed in paragraph (1).

(4) The cost per car-mile shall be calculated by adding 50 percent of the railroad's total freight-train car repair cost (R-1, Sch. 320, line 74, col. (e)); 40 percent of the railroad's total freight-train car depreciation costs (R-1, Sch. 330, line 3, col. (e)); the mileage portion of the railroad's payments for hire of time-mileage freight-train cars (R-1, Sch. 376, line 8, col. (d)) plus 50 percent of *Leased Rental—Railroad, Insurance and Other Companies* (R-1, Sch. 376, line 17, cols. (d) and (f)), *Other Basis* (R-1, Sch. 376, line 18, cols. (d) and (f)), and *Auto Racks* (R-1, Sch. 376, line 21, cols. (d) and (f)); subtracting the mileage portion of the railroad's receipts for the hire of time-mileage freight-train cars (R-1, Sch. 376, line 8, col. (c)), and 50 percent of the following lines: *Leased Rental—Railroad, Insurance and Other Companies* (R-1, Sch. 376, line 17, cols. (c) and (e)), *Other Basis* (R-1, Sch. 376, line 18, cols. (c) and (e)), and *Auto Racks* (R-1, Sch. 376, line 21, cols. (c) and (e)); and dividing the result by the total system car-miles developed in paragraph (2).

7. Add the following new paragraphs to § 1125.5:

(l) *Administrative costs*. One-half of one percent of the total annual revenues attributed to the branch shall be allowable as an avoidable cost to the railroad to cover all costs of administering the subsidy program.

(m) *Deferred subsidy payments*. If the subsidy amount is paid in deferred payments, the railroad shall be compensated for the use of its working capital by applying the interest rate established in section 1125.7 to the deferred payment for the period of time such payment is outstanding.

[FR Doc. 75-8144 Filed 3-27-75; 8:45 am]

In the Supreme Court of the United States

1976

OCTOBER TERM, 1976

MICHAEL ROBAK, JR., CLERK

COMMONWEALTH OF PENNSYLVANIA AND  
NEW YORK STATE DEPARTMENT OF TRANSPORTATION,  
PETITIONERS

v.

INTERSTATE COMMERCE COMMISSION AND  
UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO  
THE UNITED STATES COURT OF APPEALS FOR THE  
DISTRICT OF COLUMBIA CIRCUIT

BRIEF FOR THE UNITED STATES AND  
THE INTERSTATE COMMERCE COMMISSION  
IN OPPOSITION

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## In the Supreme Court of the United States

OCTOBER TERM, 1976

No. 75-1889

COMMONWEALTH OF PENNSYLVANIA AND  
NEW YORK STATE DEPARTMENT OF TRANSPORTATION,  
PETITIONERS

v.

INTERSTATE COMMERCE COMMISSION AND  
UNITED STATES OF AMERICA

*ON PETITION FOR A WRIT OF CERTIORARI TO  
THE UNITED STATES COURT OF APPEALS FOR  
THE DISTRICT OF COLUMBIA CIRCUIT*

**BRIEF FOR THE UNITED STATES AND  
THE INTERSTATE COMMERCE COMMISSION  
IN OPPOSITION**

## OPINIONS BELOW

The opinion of the court of appeals (Pet. App. 1a-21a) is reported at 535 F. 2d 91. The regulations of the Rail Services Planning Office of the Interstate Commerce Commission and the supporting reports (Pet. App. 24a-57a) are published at 40 Fed. Reg. 1624 and 40 Fed. Reg. 14186.

## JURISDICTION

The judgment of the court of appeals (Pet. App. 22a-23a) was entered on March 31, 1976. The petition for a

writ of certiorari was filed on June 29, 1976. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

#### STATUTES INVOLVED

Section 205(d)(6) and Section 304(c)(2)(A) of the Regional Rail Reorganization Act of 1973, 87 Stat. 994, 1008-1009, as amended by Sections 309 and 804 of the Railroad Revitalization and Regulatory Reform Act, Reform Act, (P.L. 94-210, 90 Stat. 59, 135), 45 U.S.C. 715(d) Pub. L. 94-210, 90 Stat. 58-59, 134-135,<sup>1</sup> are set forth at pages 3 and 5-6 of the petition.

#### QUESTION PRESENTED

Whether regulations of the Rail Services Planning Office of the Interstate Commerce Commission defining the term "avoidable costs" conform to Section 304(c)(2)(A) of the Regional Rail Reorganization Act.

#### STATEMENT

The Regional Rail Reorganization Act of 1973 (the "Rail Act"), 87 Stat. 985, 45 U.S.C. (Supp. V) 701 *et seq.*, as amended by the Railroad Revitalization and Regulatory Reform Act of 1976 ("the Reform Act"), Pub. L. 94-210, 90 Stat. 31, provides for the reorganization of eight major northeastern and midwestern railroads, under a final system plan, into a single viable system consisting of rail properties designated for transfer to a private-for-profit corporation. *Regional Rail Reorganization Act Cases*, 419 U.S. 102, 109.<sup>2</sup> The carriers' rail properties not designated for transfer are subject to a

<sup>1</sup>Unless otherwise noted, section references throughout will be to the Rail Act as amended by the Reform Act.

<sup>2</sup>The final system plan became effective on November 9, 1975, and designated rail properties were conveyed on April 1, 1976. Sections 208(a) and 303(b).

secondary planning and reorganization process. The carrier may discontinue service and dispose of such properties (*Regional Rail Reorganization Act Cases, supra*, 419 U.S. at 116-117; Section 304(a) and (b)), unless a financially responsible person (which may be a government entity) offers to subsidize service by providing a rail service continuation payment under Section 304(c) of the Act. If the offer covers the difference between the "revenue attributable" to such rail properties and the "avoidable costs" of providing rail service on such properties,<sup>3</sup> together with a "reasonable return" on the value of such properties, the rail service involved may not be discontinued or abandoned. Section 304(c)(2)(A). This provision is the cornerstone of the State and Local Rail Services Continuation Program embodied in Title IV of the Rail Act, Sections 401-403.<sup>4</sup>

Section 205(a) of the Rail Act established the Rail Services Planning Office ("RSPO") in the Interstate Commerce Commission. Section 205(d)(3) of the original Act required RSPO, by rulemaking, to "determine and publish standards for determining the 'revenue attributable to the rail properties,' the 'avoidable costs of providing service,' and 'a reasonable return on the value,' as those phrases are used in section 304 of this Act." 87 Stat. 994. Section 304 used those terms only in connection with rail service continuation subsidies. 87 Stat. 1008-1009.

<sup>3</sup>*I.e.*, avoidable by termination of service.

<sup>4</sup>Under that Program, each State in the region is entitled to receive rail service continuation subsidy assistance (Section 402) and acquisition and modernization loans (Section 403) for purposes of continuing rail services pursuant to State plans for rail transportation and local rail services (Section 402(c)(1)) under regulations issued by the Secretary of Transportation (Section 402(c)(4) and (d)). These regulations have been issued and are codified at 49 C.F.R. Part 255.



Pursuant to that mandate, on February 25, 1974, RSPO issued a notice of proposed rulemaking and order (39 Fed. Reg. 7182). After an extended period for public comment, RSPO issued initial standards on July 1, 1974 (39 Fed. Reg. 24294) and, after further comment and field testing,<sup>5</sup> issued amended standards on January 8, 1975 (Pet. App. 24a-46a), and adopted its present regulations on March 28, 1975 (Pet. App. 49a-57a).<sup>6</sup>

In order to fashion a subsidy formula that would leave room for "arm's-length negotiations between the parties," yet assure the continuation of needed service by providing a "mandatory procedure" in the event that agreement could not be reached on a voluntary basis (Pet. App. 25a-26a), RSPO first sought to develop a method for ascertaining the "revenue attributable" to particular rail properties. Because it was unable to construct what it considered to be an appropriate basis for allocating rail freight revenues to branch line operations (Pet. App. 31a), RSPO defined "revenue attributable" to such operations to include *all* system revenues earned on freight traffic *either* originating *or* terminating on the branch line, together with an allocation of passenger revenue based on the ratio of

<sup>5</sup>All interested parties were invited to participate through publication of notice of the proposal in the Federal Register and by service upon all parties of record in the rulemaking proceeding (39 Fed. Reg. 33574). See discussion in January 8, 1975, report (Pet. App. 26a).

<sup>6</sup>RSPO allowed 113 days for public comment, during which it received and evaluated more than 300 statements, before it issued its initial standards (39 Fed. Reg. 19362). The amended standards reflected experience in tests conducted at the Penn Central data collection headquarters in Philadelphia, and on two Penn Central branch lines; public seminars conducted during August and September of 1974; and comments seeking revision of the initial standards (Pet. App. 25a). Only seventeen additional comments were received after promulgation of the amended standards (Pet. App. 50a).

passenger car miles on the branch to passenger car miles on the system of railroad, to the extent such revenue is earned by passenger trains originating or terminating on the branch line (49 C.F.R. 1125.4; Pet. App. 39a-40a, 57a).<sup>7</sup>

This allocation of system revenues to the branch line affected the definition of "avoidable costs" identified with the production of those revenues. RSPO agreed with petitioners that "avoidable costs" should be strictly construed (Pet. App. 31a). However, it recognized that a narrow construction of that term does not necessarily preclude consideration of "indirect costs" (*ibid.*). Since related off-branch revenues were attributed to the branch lines, related off-branch costs were also properly attributable under the definition of "avoidable costs." RSPO stated (Pet. App. 33a):

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RSPO's decision to include all revenue earned on freight traffic either originating or terminating on the branch line represented a departure from the formula traditionally employed by the Commission in abandonment proceedings under Section 1(18) of the Interstate Commerce Act, as added and amended, 41 Stat. 477, 49 U.S.C. 1(18). That formula allocates revenue earned on freight moving over the branch line between the branch and the system, with 50 percent of the system revenue then added to the branch. Cf. *Penn Central Co. Abandonment*, 347 I.C.C. 223, 225. However, RSPO recognized that the circumstances underlying discontinuance of service and abandonment of rail properties under Section 304 of the Rail Act "are not analogous to those involved either in an abandonment proceeding under section 1(18) of the Interstate Commerce Act or in the determination of a reasonable return on an investment base necessary for the continuing discharge of common carrier obligations in the public interest" (Pet. App. 34a; see also, Pet. App. 53a), and no significant objections were raised to RSPO's definition of "revenues attributable" as finally promulgated. Petitioners here challenge only RSPO's definition of "avoidable costs" insofar as that definition includes certain elements of so-called "off-branch costs," and specifically state that they "do not quarrel with the [definition of] 'revenue attributable'" (Pet. 6).

While on the surface it might seem inconsistent to allow system variable costs to be allowed for off-branch costs, it is believed justified on the basis of equity to the railroad since all system revenues from traffic originating or terminating on the branch are attributed to the branch. A failure to recognize off-branch variable costs would probably lead to situations where the operating railroad would try to divert the traffic to another carrier at the earliest possible point regardless of service considerations. This would not only result in circuitous movement and concomitant time delays but would also decrease the revenue attributable to the branch. The adopted approach recognizes the services rendered by the carrier to the branch traffic.

Accordingly, the regulations define the "avoidable costs of providing service" to include all costs associated with handling freight traffic or providing passenger service on the branch line itself (on-branch costs) (49 C.F.R. 1125.5(a)-(j); Pet. App. 40a-44a, 57a) and, in addition, with respect to freight traffic only, certain costs associated with handling traffic originating or terminating on the branch line to the extent that such traffic moves over the remainder of the railroad's system (off-branch costs) (49 C.F.R. 1125.5(k); Pet. App. 44a).

In adopting this approach, RSPO recognized that off-branch costs would not be considered "avoidable" costs in an ordinary abandonment proceeding. It determined, however, that abandonment standards are not a valid comparison because "[t]he subsidy standards are designed in accordance with the Act to define the cost of providing service and not the cost of abandoning service" (Pet. App. 53a). The Office likewise rejected the contentions that more sophisticated bases for calculating off-branch

costs were necessary, finding that the costs associated with the installation of a systemwide cost accounting and reporting system "[could] not be justified on the basis of the subsidy program alone" (Pet. App. 29a) and that use of a system based on per diem regulations to develop car costs would be "overly complex to apply" (Pet. App. 54a).

On petitions for review,<sup>\*</sup> petitioners contended that RSPO erred in failing to follow abandonment standards, and also argued, for the first time, that RSPO was foreclosed from adopting a definition of "avoidable costs" that attributed any portion of off-branch costs to the branch line because of the Commission's interpretation of the identical phrase in regulations issued under Section 401 of the Rail Passenger Service Act of 1970, 84 Stat. 1334, 45 U.S.C. 561 ("Passenger Act").

The court of appeals, in a unanimous opinion by Judge Leventhal, rejected these contentions. It held that the legislative history of the statute did not show any congressional intent that avoidable costs "be measured by duplication of the ICC regulations under the 1970 law" (Pet. App. 9a). It agreed with RSPO that the Rail Act, with its focus on subsidized continuation of service, had a different purpose from that of both the old abandonment statute and the Passenger Act (Pet. App. 5a-9a). The court emphasized that the Rail Act required only "a clear nexus between the revenues

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<sup>\*</sup>The statute makes no provision for administrative review by the Commission of RSPO's regulations under the Act. Nevertheless since RSPO was established as an office in the Commission (Section 205(a)), its regulations were deemed to be regulations of the Commission for purposes of judicial review under 28 U.S.C. (Supp. V) 2321.



attributable to the particular line and the costs incurred in their production" (Pet. App. 9a, n. 6a) and held that RSPO's regulations established that nexus (Pet. App. 11a). Accordingly, after finding that "[t]he opposing States \* \* \* have not shown that RSPO's approach will require a significantly greater expenditure of state revenues for rail service continuation subsidies than the approaches they advocate" (Pet. App. 11a), the court rejected "the contention of the petition filed by the States that the RSPO regulation is facially invalid, without prejudice to reconsideration in light of a particularized factual showing as to the consequences of the regulation" (Pet. App. 11a).<sup>9</sup>

#### ARGUMENT

The decision of the court of appeals is correct and does not warrant review by this Court.

1. The Rail Act embodies "imaginative and innovative solutions" to a developing crisis. *In re Penn Central Transportation Co.*, 384 F. Supp. 895, 904 (Special Rail Act District Court). One such solution is a major shift in national railroad policy by which unprofitable lines may be continued in operation under state-federal subsidies, rather than simply abandoned by the railroads (Pet. 12). The measure of the subsidy is the difference between the "avoidable cost" of service and the "revenue attributable" to it, plus a reasonable return. Petitioners, as States that offer such subsidies, are interested in reducing them by keeping "avoidable costs" low and "attributable revenues" high. They contend

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<sup>9</sup>The court also held (Pet. App. 3a-4a) that a challenge by another party to the constitutionality of the Act could be determined only in the special Court created under Section 209(b) of the Rail Act, 87 Stat. 999-1000, as a result of amendments to its jurisdiction made by Section 602(b) of the Reform Act, 90 Stat. 86-87.

therefore that RSPO erred in permitting "avoidable costs" to be enlarged, for subsidy purposes, by certain off-branch costs. The court of appeals correctly recognized that the definition, on its face, comes within the broad discretion conferred on the agency by Congress.

Petitioners contend that in enacting the Rail Act Congress meant "avoidable cost" to have the precise meaning attributed to the term by the Commission in its regulations under the Passenger Act (Pet. 12-13).<sup>10</sup> But the Act's provisions for subsidized continuation of service furnished a new alternative to abandonment of failing branch lines or (as with the Passenger Act) their transfer to a government-sponsored corporation. In making such a major policy innovation, Congress could scarcely have intended to bar corresponding innovation in the rules that give life to the Act's policy.<sup>11</sup>

The pertinent language of the Rail Act, as amended by the Reform Act, itself shows that Congress did not intend RSPO to be bound by prior formulations under other statutes. Section 205(d)(3) of the original Rail

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<sup>10</sup>Those regulations, issued in a proceeding entitled *Ex Parte No. 268, Determination of Avoidable Losses under the Rail Passenger Service Act of 1970*, 343 I.C.C. 379, are codified at 49 C.F.R. Part 1123 and governed the payments required of carriers in exchange for relief from their statutory obligation to provide passenger service.

<sup>11</sup>Experience has indicated the workability of the standards developed by RSPO. Fourteen States, including both New York and Pennsylvania, have entered into rail service continuation operating agreements based upon the standards promulgated by RSPO. In total 204 branch lines involving 3,111 miles of track, including 90 branch lines and 1093.5 miles of track in New York and Pennsylvania, are being operated under such agreements.

Act (87 Stat. 994) directed RSPO to "determine and publish standards for determining the 'revenue attributable to the rail properties,' the 'avoidable costs of providing service,' and a 'reasonable return on the value' \* \* \*," as those terms were used in Section 304 to define the coverage of rail service continuation subsidies for properties not designated in the northeast region final system plan. This mandate was further enlarged by Section 309 of the Reform Act, which added Section 205(d)(6) to the Rail Act (90 Stat. 58-59). The amendment not only restated RSPO's prior responsibility to define "avoidable costs" and related terms as used in Section 304, but also directed it "from time to time [to] revise and reissue standards" for determining them. This language clearly imposes a dynamic responsibility, not a static codification of earlier concepts. Cf. *Permian Basin Area Rate Cases*, 390 U.S. 747, 776.

As petitioners note (Pet. 12), the regulations implementing the Passenger Act had already been published when Congress passed the Rail Act; had Congress meant these regulations to apply under the latter law, it could easily have said so. Instead, Congress gave the new office general authority, to be exercised after rulemaking, to "determine and publish standards for determining" avoidable cost and other key terms. 87 Stat. 994. And while the legislative history shows that Congress did not leave the matter entirely open-ended,<sup>12</sup>

<sup>12</sup>The Senate Report stated:

While the Commission would determine and publish the standards for calculating the revenues attributable to the rail properties and the avoidable costs of providing service, the Committee expects the Commission to define avoidable

that history, as the court of appeals pointed out, does not indicate that these costs should or must be measured by the Commission's regulations under the Passenger Act (Pet. App. 9a).

What the legislative history does show (n. 12, *supra*) is a congressional intention that, whatever definition might be chosen, there be "a clear nexus between the revenues attributable to the particular line and the costs incurred in their production, to exclude 'any portion of the common costs which would not be covered by revenues received by operation of a line'" (Pet. App. 9a, n. 6a). RSPO's definition meets this test. After extensive study (Pet. App. 25a-26a), RSPO concluded that it was unable to separate the on-branch from off-branch revenues of a line, and thus ruled that a line would be credited with all revenue accruing from traffic which originates or terminates on the line (Pet. App. 31a, 40a).<sup>13</sup> Since RSPO was including off-branch revenue in its "revenue attributable" standard, it reasoned that in the interest of fairness and efficiency that some off-branch costs should be included (Pet. App. 33a). RSPO carefully chose costs that contribute to the production of the pertinent revenue: terminal and/or interchange costs, and line-haul costs

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costs in such a way as to allow the Corporation or other person performing the service to recover all costs directly attributable or solely related to the costs of a particular service, but would not include any portion of common costs which operation of a line. [Emphasis added.]

S. Rep. No. 93-601, 93d Cong., 1st Sess. 37 (1973).

<sup>13</sup>Petitioners do not challenge this definition, which is to their advantage (Pet. 6). The formula also calls for the addition of an allocation of passenger revenue, but, in view of the very limited nature of passenger service, this element is not important, and is not in dispute here.



(Pet. App. 33a). Thus, as the court of appeals held (Pet. App. 9a, n. 6a), RSPO's formula establishes the required "nexus" between costs and revenue.

Since RSPO faithfully discharged its statutory duty in defining the terms set forth in the Rail Act, there is nothing to petitioners' suggestion that its regulations impermissibly differ from those defining the terms under other statutes (Pet. 15). An agency has the authority to change prior interpretations of the same statute, provided it gives a reasoned explanation for doing so. *American Trucking Associations, Inc. v. Atchison, T. & S.F.R. Co.*, 387 U.S. 397, 416; *Atchison, T. & S.F.R. Co. v. Wichita Board of Trade*, 412 U.S. 800, 808. The agency's latitude is much greater when it offers a different interpretation of a phrase common to separate statutes with different histories and purposes. As the court of appeals recognized (Pet. App. 6a-10a), regulations issued under the old abandonment statute and the Passenger Act do not affect the validity of different regulations under the Rail Act. Moreover, the construction of the statute by RSPO (Pet. App. 8a-9a), as the agency charged by Congress with setting the new administrative machinery in motion, is entitled to great weight. *Udall v. Tallman*, 380 U.S. 1, 16; *Train v. Natural Resources Defense Council*, 421 U.S. 60, 67, 75.

Since Congress did not bind RSPO to adopt the standards for "avoidable costs" developed in abandonment cases under prior law, petitioners' contention (Pet. 12-14) that there cannot be one definition of "avoidable costs" for subsidy purposes and another for abandonment purposes is beside the point. RSPO's present standards for purposes of service continuation subsidies under the original Rail Act may or may not prove suitable for discontinuance or abandonment purposes under the amended Rail Act, or under the changes in the Interstate Commerce Act adopted in the Reform Act. This

is a matter to be explored in future joint rulemaking by RSPO and the Commission, subject to judicial review on petition by those aggrieved.<sup>14</sup>

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<sup>14</sup>Section 304(a)(2)(A), added to the Rail Act by Section 804 of the Reform Act (90 Stat. 133-134), provides that rail service may be discontinued on rail properties not included in the northeastern region final system plan, and not otherwise designated for use under the Rail Act, "if the Commission determines that such rail service on such rail properties is not compensatory \* \* \*." For purposes of this provision, the statute provides that service is compensatory if revenues attributable to the line equal or exceed avoidable costs plus a reasonable return on the value of the properties, "as determined in accordance with the standards developed [by RSPO] pursuant to section 205(d)(6) of this Act." Section 304(a)(2)(B), 90 Stat. 134. The Commission is therefore responsible for determining when service is compensatory, and RSPO for defining the statutory terms.

But the fact that the Commission may be called upon to apply RSPO standards developed for subsidy computation purposes in passing upon applications for authority to discontinue service under Section 304(a)(2) does not, as petitioners contend (Pet. 13), demonstrate that such standards are inappropriate for the purpose for which they were developed. In any event, no applications for authority to discontinue service under this provision have been filed to date and few, if any, are anticipated prior to its expiration on November 9, 1976 (Section 304(a)(2)(A)(ii)).

While the provisions of amended Section 304(a)(2) apply only to a few of the lines in the northeastern region subject to the Rail Act, Section 802 of the Reform Act amends the procedure for discontinuances and abandonments of lines in other parts of the country. A new Section 1a has been added to the Interstate Commerce Act, which provides for discontinuance and abandonment and for the continuation of rail freight service, if financial assistance is offered which covers the difference between "revenues attributable" to the line and "avoidable costs", plus a reasonable return. 90 Stat. 127-130. As used in this provision, "avoidable costs" is defined by the statute to mean "all expenses which would be incurred \* \* \* in providing a service which would not be incurred \* \* \* if such service were discontinued or \* \* \* if the line \* \* \* were abandoned." Section 1a(10), 90 Stat. 130. The Commission, not RSPO, is responsible for applying the formula to calculate the net of "avoidable costs" plus

2. There are additional reasons that render further review inappropriate at this time. The court of appeals correctly found (Pet. App. 11a) that petitioners had failed to establish that RSPO's standards will require a "significantly greater" expenditure of state funds for rail service continuation subsidies than the approaches they advocated.<sup>15</sup> Moreover, the court made clear that petitioners will be entitled to reconsideration if they can make a particularized factual showing regarding adverse consequences resulting from RSPO's revenue-cost formulation as applied. Following any such reconsideration, the issues could be considered on the basis of "a much more developed record" confined to "particular situations." Cf. *Regional Rail Reorganization Act Cases*, *supra*, 419 U.S. at 146, and cases cited therein.

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"return on value" over "revenues attributable" for subsidy purposes (Section 1a(7), 90 Stat. 129), although RSPO retains responsibility for defining avoidable costs for purposes of Section 1a under Section 205(e)(1)(B) of the Rail Act, as added by Section 309 of the Reform Act (90 Stat. 59).

<sup>15</sup>It is also by no means clear that RSPO's approach will require an expenditure *any* greater than that which would have been required had the Commission's traditional revenue/cost formulation been adopted. Under the traditional formulation used in abandonment cases only 50 percent of the revenues earned on traffic moving beyond the branch line would be attributed back to the branch line, the remainder being deemed to be absorbed by costs associated with handling the traffic over the balance of the system. Under RSPO's formulation, on the other hand, all of the revenues are attributed to the branch line and an attempt is made to ascertain the costs incurred by the system in earning those revenues. While the latter approach should result in a more accurate allocation of costs and revenues, there is no basis at present for asserting with confidence that one or the other approach increases the amount of subsidy required to provide for continued branch line operations. Petitioners would apparently favor recognition of all of the revenues and none of the costs associated with operations beyond the branch line (Pet. 6), but such an approach would plainly be unfair to the subsidized railroad.

## CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted.

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